The Economist

AUGUST 22ND–28TH 2009 Economist.com

America's health-care battle

Cameron the brave, maybe

The shape of the recovery

The sad decline of BT

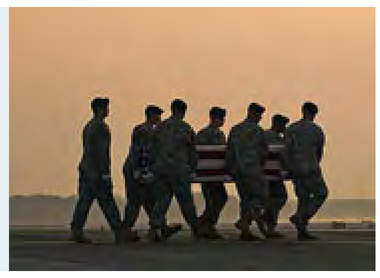
Champagne's bubble bursts

Afghanistan

The growing threat of failure

Print edition August 22nd 2009

Afghanistan
To stop the country sliding out of control, the West needs more men and a better strategy: leader



The world this week

Politics this week
Business this week
KAL's cartoon

Leaders

The war in Afghanistan
Losing Afghanistan?

Japan's election
Out with the old

World economy
U, V or W for recovery

American health care
Keep it honest

Britain's Conservatives
Step forward, Dave the brave

Letters

On energy, Jimmy Carter, efficiency, Uganda's oil, Asian-Americans, home-schooling, lavatories

Briefing

Afghanistan
From insurgency to insurrection

American opinions on Afghanistan
A war of necessity?

United States

Health reform
The labours of Sisyphus

Youth unemployment
Left behind

Drinking laws
The 21 Club

The worst unemployment figures
Benefits and the border

Gay-marriage laws
Still waiting

Robert Novak
The prince of darkness

Statewatch: Maryland
Thanks be to DC

Lexington
Still crazy after all these years

The Americas

Venezuela's education "reforms"
Hugo Chávez seeks to catch them young

Ecuador's education reforms
Correa's curriculum

The Turks and Caicos loses independence
A very British coup

Asia

Japan's election
Railing against the wrong enemy

Taiwan's typhoon
The political storm

Kim Dae-jung and North Korea
A glint of sunshine

India's failing monsoon
It never rains

Australia's relations with China
Different approaches

Previous print editions

Aug 15th 2009
Aug 8th 2009
Aug 1st 2009
Jul 25th 2009
Jul 18th 2009

More print editions and covers »

Subscribe

Subscribe to the print edition
Or buy a Web subscription for full access online
RSS feeds
Receive this page by RSS feed

Business

Consumer goods in the recession
The game has changed

Reader's Digest declares bankruptcy
Unsexy and unsuccessful

Publishing in Australia
Copyrights and wrongs

Volkswagen and Porsche
My other car firm's a Porsche

Competition comes to Mexican telecoms
Talking and saving

Cathay Pacific, Air China and Citic Pacific
Landing rights

A row in the champagne industry
Corks at dawn

Face value
Bank to square one

Briefing

BT's pension problem
Friends, family and grandads too

Finance and Economics

America's housing market
Where it all began

Housing derivatives
Spark of invention

Monetary policy
Tight corners

South Africa's economy
Late starter

Carbon markets in China
Verdant?

Reforming finance: Resolution regimes
Fail-safe

Payment cards and the poor
A plastic prop

Economics focus
The unkindest cuts

Science & Technology

Better vaccinations
Hypodermic needless

Influenza vaccination
How to stop an outbreak

The smell of death
The dogs have had their day

Reading bar codes with mobile phones
Snap it, click it, use it

Correction: Lightyears

Books & Arts

Political philosophy
Mightier than the sword

American conservatism
Overdoing it

Brazilian literature
The slide towards insecthood

New film: "District 9"
Prawns and other illegal aliens

A murder in China
Crime and punishment

China's drink-driving crackdown
Call a cab

Middle East & Africa

Libya and Muammar Qaddafi, 40 years on
How to squander a nation's potential

Israeli politics
Bibi the happy juggler

More bombings in Iraq
Lethal and relentless

An Ethiopian singer freed
Movement of jah people

Zambia's corruption trial
Not guilty

Europe

Former Yugoslavia patches itself together
Entering the Yugosphere

Germany's election
The parties' tax tangle

Dangerous dogs in Denmark
Shoot the puppy!

Russia and Ukraine
Dear Viktor, you're dead, love Dmitry

Spanish soccer
The drain to Spain

The euro-area economy
Growing apart?

Britain

An interview with David Cameron
The man who would be prime minister

Transatlantic rift over the NHS
Healthier than thou

Rebuilding Jaguar Land Rover
Tata takes charge

A-level results
Dumbing down: discuss

Children in prison
Growing up banged up

Bagehot
The vanity of ideas

Articles flagged with this icon are printed only in the British edition of *The Economist*

International

Piracy and private enterprise
Splashing, and clashing, in murky waters

The Lockerbie decision
A long shadow

The Tiananmen uprising
Spied from the inside

Les Paul
The man who changed rock music

Obituary

Gayatri Devi

Economic and Financial Indicators

Overview

Output, prices and jobs

The Economist commodity-price index

The Economist commodity-price index

Trade, exchange rates, budget balances and interest rates

Markets

Share prices by industry

Politics this week

Aug 20th 2009
From The Economist print edition

Truck bombs, mortar and rocket attacks in the **Iraqi** capital Baghdad killed around 100 people in a single day and injured more than 500 in the worst incidence of violence so far this year. Insurgents targeted heavily defended government offices and ministries, almost completely destroying the foreign ministry. More violence is expected in the run-up to elections in January. American troops pulled out of Iraq's towns in June. See article

Responding to pressure from the Obama administration, the **Israeli** government stopped issuing contracts for the construction of settler houses in the West Bank. Barack Obama welcomed the move, but the settlers said that private-sector building work will continue. See article

In **Zambia**, Frederick Chiluba, a former president, was cleared of corruption charges after a long court case. It was the first time that a former African head of state had faced a credible trial in his own country for such offences. See article

At the polls

EPA

As **Afghanistan** went to the polls in a presidential election, suicide-bombings and other violence continued in parts of the country, including the capital, Kabul. A bank was raided close to the president's compound. See article

In **Pakistan**, the army arrested a man it described as the chief spokesman for the Pakistani Taliban. It said he confirmed that the group's leader, Baitullah Mehsud, had indeed been killed, as American and Pakistani officials had claimed.

The suffering of nearly 300,000 people interned in camps in northern **Sri Lanka** since the end of the war against the Tamil Tigers was worsened by heavy rains and severe flooding.

India's main opposition, the Bharatiya Janata Party, expelled one of its senior members, Jaswant Singh, a former foreign and finance minister, for publishing a book that praises Muhammad Ali Jinnah, the founder of Pakistan.

Kim Dae-jung, a former president of **South Korea**, died aged 85. He was known for his "sunshine policy" of pursuing engagement with North Korea, which said it would send a delegation to his funeral. Separately, in a meeting with a South Korean businesswoman, Kim Jong Il, the North Korean dictator, promised to allow a reunion for some separated Korean families, to permit South Korean tourists back into the country, and to renew commercial ties. See article

The number of people known to have died in **Taiwan** in the devastation caused by Typhoon Morakot reached about 500. The president, Ma Ying-jeou, apologised for the perceived failures of the government's rescue effort. See article

The campaign opened for **Japan's** general election on August 30th. Opinion polls suggest that the ruling Liberal Democratic Party, which has been in power almost continuously for half a century, faces defeat by the opposition Democratic Party of Japan. See article

The nuclear option

The debate over **health-care reform** focused on just how vigorously the White House would push for the "public option" of government-run insurance. Such a scheme is included in legislation that has emerged from Congress so far, and is strongly favoured by many Democrats. Some in the Obama administration suggested it could be ditched in order to reach a compromise with Republicans. See article

There were more angry scenes at **town-hall meetings**. One congressman told a protester that attempting to reason with her about health care would be like "trying to argue with a dining-room table". American conservatives attacked Britain's National Health Service, calling it "evil". Stephen Hawking recently rubbished a claim that he "wouldn't have a chance" under the British system with his debilitating disease. The renowned physicist was treated by the NHS.

California's lawmakers returned to work after their recess, with Democrats hoping to tweak some of the severe cuts to social services announced in last month's budget deal. A state board voted to end health insurance for more than 60,000 children because of the budget amendments.

Senator Kay Bailey Hutchison launched her campaign for governor of **Texas**, throwing down a strong challenge to Rick Perry, the incumbent. Mrs Hutchison is a Republican moderate (for Texas) and thinks Mr Perry, who succeeded George Bush in 2000, has been in the governor's mansion for too long. The Republican primary will be held in March.

Trouble in paradise

Britain removed the elected government and assembly of the **Turks and Caicos** islands, an overseas territory in the West Indies, and reimposed direct rule from London, after an official inquiry found signs of "systemic corruption". See article

Venezuela's parliament, dominated by supporters of President Hugo Chávez, rushed through a controversial education law under which school lessons will be based on "Bolivarian doctrine". See article

A group of Catholic bishops from the United States visited **Cuba** and urged both countries' governments to "listen to their better angels" and seize the opportunity to bring an end to 50 years of hostilities between them.

Figures showed that new passport controls which the United States imposed on its border with **Canada** in June have caused a sharp drop in cross-border travel.

A riot involving rival gangs in a prison in **Mexico** left 19 inmates dead.

Mystery ship

AFP

Russia said that it had found a **hijacked merchant ship** that had gone missing in the Baltic Sea on July 30th en route to Algeria. The *Arctic Sea* was located in the Atlantic, 300 miles off the Cape Verde islands. Its disappearance had sparked a worldwide hunt as well as rumours of piracy in the English channel, mafia disputes and illegal cargoes which the ship's reappearance did not lay to rest.

A bomb killed more than 20 people outside a police station in Nazran, the capital of the Russian province of **Ingushetia**. It was the bloodiest so far in a series of bombings to have hit the Caucasian republics.

Georgia became the first member formally to leave the Commonwealth of Independent States, a trade block formed in 1991 by former Soviet republics to cushion the economic blow of the Soviet Union's collapse.

Business this week

Aug 20th 2009
From The Economist print edition

UBS made public the terms of its settlement with the Internal Revenue Service after a tax-evasion investigation. The Swiss bank will give the American agency the names of 4,450 clients suspected of hiding assets in their accounts, who will be encouraged to join the IRS's "voluntary disclosure" scheme. UBS will not be fined. Some in Switzerland fret that the deal undermines the country's reputation for banking secrecy. But the government reckoned the announcement lifted a cloud over UBS and sold the SFr6 billion ($5.6 billion) investment it made in the bank last year to help it through the financial crisis.

Pay differentials

American International Group disclosed that Robert Benmosche, its new chief executive, will be paid $7m in cash and shares. He recently took charge at the troubled insurer after the retirement of Edward Liddy, who was paid a nominal $1 when he was given the job amid AIG's bail-out. The Treasury's pay tsar has approved "in principle" to Mr Benmosche's pay package.

A panel of appeals-court judges overturned the 2007 conviction of Gregory Reyes on charges related to the illegal **backdating of share options** and ordered a retrial. The case against Mr Reyes, a former boss of Brocade Communications Systems, was the most high-profile in a spate of share- options scandals that came to light in 2006. Studies have since found that only a fraction of illicit payments were revealed. The appeals-court panel said that in Mr Reyes's case, prosecutors had misled the jury into thinking Brocade was unaware of the practice.

It emerged that Mervyn King, the governor of the **Bank of England**, had wanted to pump an extra £75 billion ($125 billion) into the British economy through his "quantitative easing" programme rather than the £50 billion that the Monetary Policy Committee approved earlier this month. The normally cautious Mr King had argued that the recovery was very fragile and could do with a bigger boost.

Karma chameleon

MySpace bought **iLike**, a music-recommendation service that is popular on rival websites. With the rise of Facebook, MySpace is retuning its business so it looks less like a social-networking site and more an entertainment portal.

Hewlett-Packard's quarterly profit fell by 19%, as demand for its products fell. But the company was upbeat, stating that its business has "stabilised" after companies and consumers made huge cuts in their technology spending at the start of the recession.

Volkswagen outlined its proposed merger with **Porsche**. The deal is complex but should see the controlling Piëch and Porsche families holding 40% of the combined firm, with the German state of Lower Saxony and Qatar's sovereign-wealth fund each taking around 20%. See article

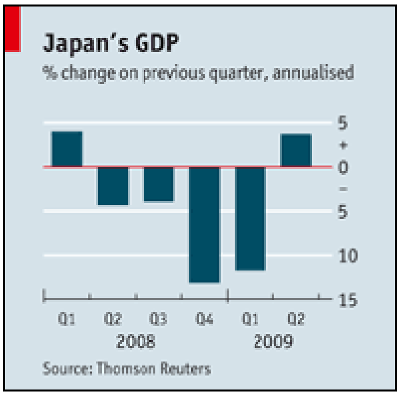
General Motors said it was increasing production and hiring workers at two factories in response to extra business generated by the government's **"cash-for-clunkers"** scheme. But the programme will soon end and some question whether the uptick in demand will continue once the subsidies are withdrawn.

Japan's economy grew in the second quarter, largely because of a rise in both exports and government spending. Experts warned that underlying pressures, such as deflation and unemployment, could tip Japan back into recession. See article

The **Shanghai Composite Index** slid again. China's benchmark stockmarket has fallen by 20% since early August, when it reached a high for the year. One factor fuelling the decline is the government's directive to

tighten excessive lending practices, which has unsettled China's legions of retail investors.

PetroChina signed a contract to buy **liquefied natural-gas** from Exxon Mobil's supplies in the Gorgon field off Western Australia. The Australian government said the agreement was worth A$50 billion ($41 billion), Australia's biggest-ever trade deal. See article



On the shelf

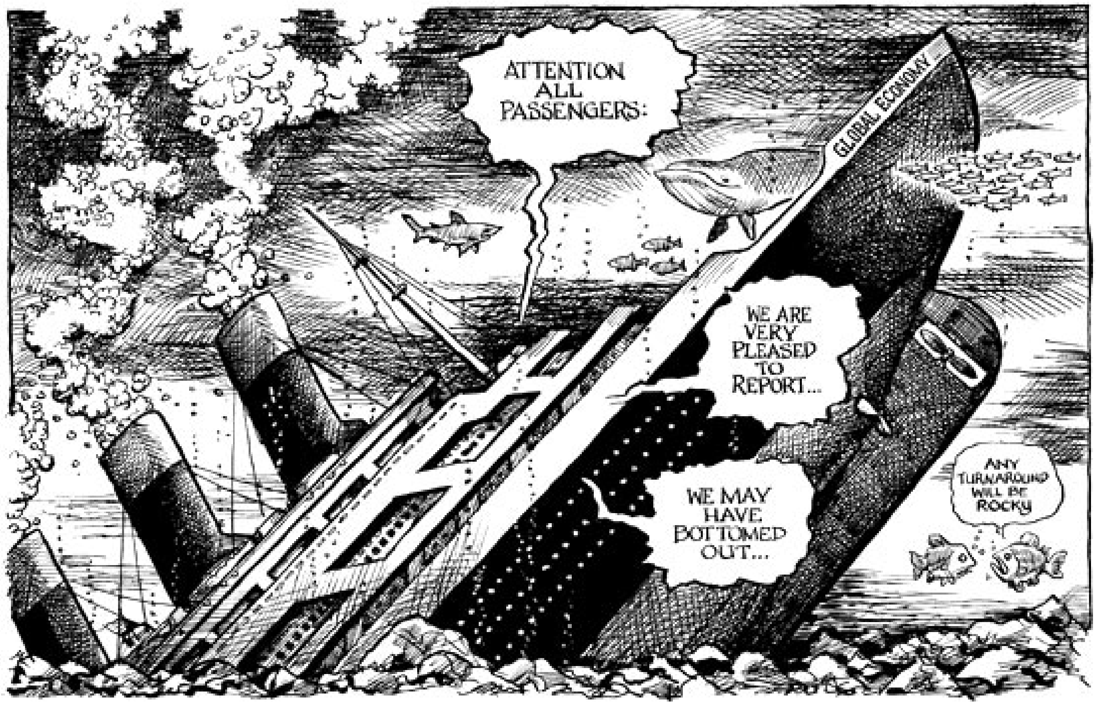
Reader's Digest Association laid out plans to enter bankruptcy protection. In addition to its popular monthly magazine, the company's titles include *Birds & Blooms*, *Country Woman* and *Our Canada*. It was bought by a private-equity firm two years ago, but like others in the publishing industry has struggled with debt and lower advertising revenues. See article

America's Justice Department charged a man in what it said was the biggest-ever case of **identity theft** in the United States. Albert Gonzalez allegedly stole information on 130m credit and debit cards from the computers of several retailers, including 7-Eleven. Known online as "soupnazi", Mr Gonzalez once worked with the Secret Service, helping track down computer hackers.

KAL's cartoon

Aug 20th 2009
From The Economist print edition

Illustration by KAL



Losing Afghanistan?

Aug 20th 2009
From The Economist print edition

To stop the country sliding out of control, the West needs more men and a better strategy

AFP

THIS is the just war, the "war of necessity", as Barack Obama likes to put it, in contrast to the bad war, the war of misguided choices in Iraq. But as a deeply flawed election went ahead in Afghanistan this week, there were echoes, in the mission by America and its allies, of the darkest days of the Iraq campaign: muddled aims, mounting casualties and the gnawing fear of strategic defeat. Gloomy commentators evoke the spectre of the humiliations inflicted by Afghanistan on Britain in the 19th century and the Soviet Union in the 20th.

Americans, relieved to be getting out of Iraq, and caught up in a national row about health care, are paying little attention to the place. But if things there continue to slide, Afghanistan could turn out to be the biggest blot on the Obama presidency.

Why the West is there

The war is going badly. Much of the south of the country is out of government control. A scattered, disparate insurgency has gained strength and risks turning into a widespread insurrection against Western forces and the elected government they are backing (see article). In Britain, a sceptical public wonders what its soldiers are dying for. And as the costs and casualties continue to mount, Americans too will ask that question increasingly loudly (see article).

Western governments use a lazy shorthand to justify this war. Its purpose, they say, is to deny terrorists the base and haven that Afghanistan under the Taliban provided to al-Qaeda. But al-Qaeda's surviving leaders are reckoned to have decamped across the border to the tribal areas of Pakistan, where Western forces do not tread. The other reasons that Western governments keep their soldiers in Afghanistan are harder to sell to voters: first, because a precipitate departure would damage the West's global clout, and, second, to stop the country becoming the theatre for a war which could destabilise Pakistan and draw in other powers, such as Iran, India and Russia.

As the West struggles to maintain its weak hold on Afghanistan, so its ambitions there are narrowing. Early aspirations to bring peace, prosperity and decent government to the country have been replaced by the hope of establishing a functioning state and of improving security. By that measure, success in the short term will look much like stalemate. But the chance of achieving even these modest aims is being

jeopardised by too few troops and a flawed strategy.

The shortage of soldiers has hampered the generals' ability to hold territory and forced them to use air power to make up for the lack of numbers. The civilian casualties that are the inevitable consequence of conducting a war from the air are, in turn, damaging the war effort. The generals need more troops both to regain territory from the Taliban and to fight the war in a way that does not breed hostility to the West.

Yet swamping Afghanistan with foreign soldiers will never bring outright military victory. The surge that helped secure Baghdad was carried out in a smallish, densely populated area. Such tactics cannot be contemplated in a country as mountainous and rural as Afghanistan. If the West is to stop the place slipping further out of control, it needs not just to direct more resources to the place, but also to use them better. That means different approaches to three elements: the opposition, the government and aid.

The opposition, casually described as "the Taliban", is far from a unified force in a country of great ethnic complexity. It includes not just religious zealots but all manner of tribal warlords and local strongmen. Many have alarming ideas and repellent social attitudes. But if Afghanistan is to be stabilised, the West will have to hold its nose and encourage its allies in government to do deals with them.

On the campaign trail, President Hamid Karzai has appealed to his enemies to make peace. But his government—inept, corrupt and predatory—does not look like a trustworthy partner. In parts of Afghanistan where insurgents have been driven out and the writ of the government has been restored, residents have sometimes hankered for the warlords, who were less venal and less brutal than Mr Karzai's lot.

Cleaning up government is not just an end in itself but also a means to building a functioning state, for Afghans will not support an administration as corrupt as the current one. The West should therefore use its leverage over the government to insist that the next cabinet is dominated by competent technocrats, rather than thugs owed a favour.

How to spend it

The West is spending a fortune in aid to Afghanistan. As the new head of Britain's army recently pointed out, it is likely to have to go on supporting the country for decades. Yet the roads that are foreign development's proudest boasts also serve to meet the insurgents' and drug-dealers' logistical needs.

That is inevitable: infrastructure serves the wicked as well as the righteous. But the West has not spent its money as well as it could have. By giving too many contracts to foreigners, it has created grudges instead of buying goodwill. To most Afghan eyes, watching heavily guarded foreign aid-workers glide by in their Landcruisers, it is obvious that much of the money is going straight back out of the country. To a degree, this is forgivable: in such a poor country it is difficult to build the capacity to manage huge volumes of aid, and channelling more of the cash through the government may mean that more of it gets stolen. But that is a risk that needs to be taken to build support for the West and the government.

Taking even the rosiest view, the war in Afghanistan is likely to get more expensive, and worse, before it gets better. The mini-surge this year to enable the election to take place in most of the country will probably be followed by another to try to contain the growing insurgency. For the moment, Mr Obama is better off than George Bush was when Iraq went bad, because he enjoys broad political and popular support for this commitment. But as casualties mount, political pressure in America to announce a timetable for military withdrawal will intensify. To resist it, Mr Obama will need more men, a better strategy and a great deal of luck.

Japan's election

Out with the old

Aug 20th 2009
From The Economist print edition

The Liberal Democratic Party is on the brink of electoral defeat. About time too

Reuters

ONE of the longest leases on power in the post-war era looks likely to end on August 30th. In Japan's curiously genteel election campaign, opinion polls indicate that the ruling Liberal Democratic Party (LDP) is heading for defeat. This would only be good for Japan. The LDP, in power almost without interruption since 1955, is a cold-war relic. Its days have been numbered since the collapse of the Berlin Wall coincided with the bursting of Japan's bubble economy.

What good the party did in helping build one of the world's mightiest and most egalitarian industrial nations is now almost ancient history. In recent years it has played a sordid game, lavishing favours on those—such as exporters, builders and farmers—whose votes and money have kept it in power. Its unseemly ties with the country's famously conservative bureaucracy have prevented it from tackling Japan's pressing social problems. In an ageing society where many pensioners are refreshingly sprightly, the ruling party looks utterly clapped-out.

A pity then that the party that looks likely to win the most seats in the lower house, the Democratic Party of Japan (DPJ), looks so callow and ill-prepared to take over. For all the applause that greeted the release of its rather radical manifesto last month, it has—after meetings with its rank-and-file—meekly watered it down. It has inserted a clause, for instance, that in effect ensures Japan's cosseted farmers would be exempt from any free-trade deal with America.

Its leader, Yukio Hatoyama, who may well be the next prime minister, has managed to bungle the message on matters as delicate as Japan's long-standing military ties to the United States. Most troubling, in a recent tirade against what he called American-led "market fundamentalism", he not only attacked the deregulation carried out by Junichiro Koizumi, a former prime minister, earlier this decade (see article), but also wanted to burden business with more rules.

Despite the news that GDP growth resumed in the second quarter, unemployment is rising and wages are falling. So this might play well to the gallery. What politician doesn't these days profess concern about the sharp elbows of American capitalism? But Mr Hatoyama and his party have got the wrong end of the stick. It wasn't Mr Koizumi's reforms that devastated Japan's economy and caused soaring rates of poverty and inequality. Those trends, though they have worsened this year, date further back, to the "lost decade" of the 1990s.

Lionheart's lacunae

Mr Koizumi’s reforms fell short for a more subtle reason. He was right to free up employment in the export sector, giving it more scope to hire and fire; it has to compete globally. But he should have also built up the welfare state to catch those dislocated by the swings in the business cycle. And Japan’s trussed-up services industry, which accounts for a much larger share of jobs than does the export sector, is in sore need of further deregulation. That would allow new businesses to start and productivity to flourish.

Elections, however, are no time for subtlety. Other aspects of the DPJ’s platform, such as an assault on the power of the bureaucracy, are well worth the applause. If it can impose its will on civil servants, it might be able to break through the inertia that has prevented Japan from sorting out its pensions crisis and dealing effectively with an ageing society. That, however, depends on economic growth. And the DPJ verges dangerously close to believing that this matters less than the redistribution of wealth. Once the DPJ has kicked out the LDP, it should kick that foolish notion, too.

World economy

U, V or W for recovery

Aug 20th 2009
From The Economist print edition

The world economy has stopped shrinking. That's the end of the good news

IT HAS been deep and nasty. But the worst global recession since the 1930s may be over. Led by China, Asia's emerging economies have revived fastest, with several expanding at annualised rates of more than 10% in the second quarter. A few big rich economies also returned to growth, albeit far more modestly, between April and June. Japan's output rose at an annualised pace of 3.7%, and both Germany and France notched up annualised growth rates of just over 1%. In America the housing market has shown signs of stabilising, the pace of job losses is slowing and the vast majority of forecasters expect output to expand between July and September. Most economies are still a lot smaller than they were a year ago. On a quarterly basis, though, they are turning the corner.

This is good news. The first step in any recovery is for output to stop shrinking. But the more interesting question is what shape the recovery will take. The debate centres around three scenarios: "V", "U" and "W". A V-shaped recovery would be vigorous, as pent-up demand is unleashed. A U-shaped one would be feebler and flatter. And in a W-shape, growth would return for a few quarters, only to peter out once more.

Optimists argue that the scale of the downturn augurs for a strong rebound. America's deepest post-war recessions, they point out, were followed by vigorous recoveries. In the two years after the slump of 1981-82, for instance, output soared at an average annual rate of almost 6%; and this time round, output has slumped even further, and for longer, than it did in the early 1980s.

Pessimists, meanwhile, think this downturn's origins favour a weak recovery or a double-dip. Unlike typical post-war recessions this slump was spawned by a financial bust, not high interest rates, and when overindebted borrowers need to rebuild their balance-sheets and financial systems need repair, growth can be weak and easily derailed for years. Japan's 1990s banking crisis left the economy stagnant for a decade; a premature tax increase in 1997 plunged it back into recession.

V for vulnerable

Neither of these parallels is exact, because today's global slump combines several types of downturn and an unprecedented policy response. In formerly bubble economies, it is largely a balance-sheet recession. Debt-fuelled consumption has been felled. But the scale of collapse was broadened and deepened by the freezing up of the machinery of global finance, a dramatic collapse in confidence and stock-slashing. It was then countered with the biggest stimulus in history. The shape of the recovery depends on how these forces interact.

In the short term that shape could look beguilingly like a "V", as stimulus kicks in and the inventory cycle turns. In emerging Asia, the unfreezing of trade finance, a turnaround in stocks and hefty fiscal stimulus are powering a rebound. Government support, especially employment subsidies and incentives toa buy new cars, has cushioned demand in Germany and France (see article). With export orders rising and confidence growing, the next few months could be surprisingly buoyant. Even in America, the fiscal stimulus is kicking in, the "cash for clunkers" scheme is a big, if temporary, prop to output and firms will, sooner or later, stop cutting inventories.

Yet a rebound based on stock adjustments is necessarily temporary, and one based on government stimulus alone will not last. Beyond those two factors there is little reason for cheer. America's housing market may yet lurch down again as foreclosures rise, high unemployment takes its toll and a temporary home-buyers' tax-credit ends (see article). Even if housing stabilises, consumer spending will stay weak

as households pay down debt. In America and other post-bubble economies, a real V-shaped bounce seems fanciful. Elsewhere, it will happen only if vigorous private domestic demand picks up the baton from government stimulus. In Japan and Germany, where joblessness has further to rise, that seems unlikely any time soon. The odds are better in emerging economies, especially China. But even there an array of reforms, from a stronger currency to an overhaul of subsidies, is needed to boost labour income and encourage consumption. Until that shift takes place, the global recovery will be fragile and probably quite feeble. A gloomy U with a long, flat bottom of weak growth is the likeliest shape of the next few years.

American health care

Keep it honest

Aug 20th 2009
From The Economist print edition

Rationing is not a four-letter word

Reuters

BLAME it on the weather or the silly-season absence of more serious news, but arguments about America's health care have become a touch delirious over the past couple of weeks. People have accused each other of being evil-mongers, dealers in death or even un-American; a sad substitute for a thoughtful debate about a complicated subject that intimately affects every citizen and ties up some $2 trillion a year, a seventh of the world's largest economy.

Now the distemper has spread across the Atlantic. The enemies of Barack Obama's health-reform plans have no more potent weapon, it seems, than to accuse him of seeking to replicate Britain's dreaded National Health Service on American soil. Even David Cameron has been dragged into the affair. An unhelpful Conservative MEP has been caught joining in the NHS-bashing in America, leading to the predictable and unfair charge that Mr Cameron's henchmen are secretly bent on unravelling the system.

This focus on the NHS is unfortunate in a couple of serious ways. First, by painting an inaccurate picture of the British system, it helps blind Americans to weaknesses in their own one that need to be corrected if it is not to collapse under the weight of its costly inefficiencies. Americans have been fed, during the summer slanging, a diet of ludicrous untruths: that the astrophysicist Stephen Hawking, for instance, would have been abandoned to die of his motor neurone disease had he been unfortunate enough to live in Britain. (He does.) More dangerous was the remark of Charles Grassley that his fellow senator, 77-year-old Edward Kennedy, would not be treated for his brain cancer if he lived in Britain on account of his age. Mr Grassley, through his position on the most important of the Senate committees considering health reform, holds its fate in his hands.

It's not so bad in Britain

The reality which these calumnies obscure is that the NHS costs half as much per person as the American system costs. Yet it delivers results which are on some plausible measures (see article) actually superior, for instance in terms of health in middle-age or life expectancy at birth (America's record at treating cancers is much better, though). And it does this while avoiding the disgrace that so shames America, of leaving around 46m people, some 15% of its population, without any form of health insurance and therefore reliant on emergency-room care, which is costly and inefficient. Many millions more are covered by only bare-bones policies, which can leave them destitute in the event of prolonged illness. But if American politicians peddle falsehoods about what goes on in other countries, Americans are correspondingly less likely to appreciate the extent to which they are being let down.

The second thing to lament about the current apology for a debate is that it is giving the idea of

controlling health-care costs a bad name. Mr Obama promised that his reform package would bring down costs, as well as extend coverage. But so spooked has the administration become by accusations of “rationing” health care, as is done in “socialist” systems like the NHS, that very little cost control is now to be expected from whatever bill eventually emerges (see article).

The reality is that America, like Britain, already makes extensive use of rationing. Around half of all Americans are covered by one government programme or another, including those providing health-insurance for the elderly, the poor and government employees. These schemes lay down in great detail, in the form of national and local “coverage determinations”, which treatments and procedures can be claimed for, and at what rates. And all but the most expensive private insurance policies impose limitations of their own. A more honest discussion would accept that cutting costs, as the administration has promised to do, must involve reining in a system that encourages patients to demand tests and procedures that they don’t really need and doctors to recommend them.

Britain's Conservatives

Step forward, Dave the brave

Aug 20th 2009
From The Economist print edition

What David Cameron needs to do between now and the general election to prove he is ready to govern

AP

SCANDALS may erupt. Terrorists could strike. Leaders can fall under buses or victim to party coups. Economic systems occasionally implode. One way or another, British politics may yet be convulsed before the general election that is due by next June. But at the moment it looks likely that the Conservative Party will win it (despite the huge electoral swing it requires), and that David Cameron, the Tory leader, will be Britain's next prime minister. It is less clear that he is ready to deal with the challenges that would confront him.

Considering all of the recession's other casualties, there may not be much compassion left over for inconvenienced politicians. But in his own way, Mr Cameron has been a victim of the credit crunch and the downturn too. Before they struck he was merrily marketing himself as an updated version of Tony Blair, pledging to pursue many of the ex-prime minister's policies, only more determinedly. After the frustratingly electable original Blair made way for cack-handed Gordon Brown, and with voters increasingly sick of Labour, this pitch looked enough to see Mr Cameron into Number 10. Suddenly, with unemployment heading for 3m, a huge deficit and national debt nudging £1 trillion ($1.7 trillion), he faces a different and more daunting task. Contrary to his expectations and perhaps his temperament, Mr Cameron must be bold.

Where the axe falls

The Tories' performance over the financial crisis and the recession has been decidedly mixed. They seemed self-interested and querulous over Northern Rock, the first British bank to wobble. They mistakenly opposed part of the government's fiscal stimulus. A Prime Minister Cameron, however, would probably inherit a recovering economy rather than a contracting one; and some of the Tories' ideas for this scenario, on bank regulation for example, have been more convincing. Asked about Barack Obama's experience in our interview (see article), Mr Cameron suggests the lesson may be that new leaders can't pursue too many goals at once. His priority, he claims, will be to shrink Britain's deficit and reduce its debt.

A sound aim—a shame, then, that he has yet to explain how he would go about it. Compared with Mr Brown, who pretends that public spending can magically continue to rise (despite Treasury forecasts to the contrary), Mr Cameron has been frank about the need to trim it. But his candour is only relative.

He has said his emphasis would be on spending cuts rather than tax rises (though those are not ruled

out). He and George Osborne, the shadow chancellor, have identified a few programmes to axe, such as Labour's pointless identity-card scheme, some costly databases and the odd quango: things few people cherish or would miss. Yet the implied savings are tiny beside the task Mr Cameron has set himself. The Tories have some sensible plans for the public services, notably schools; but these are unlikely to save cash for several years, and will require upfront lubrication. They have talked toughly but vaguely about reining in public-sector pay and pensions; it remains to be seen whether they have the gumption to face down the union-led unrest such a squeeze would provoke.

Mr Cameron, in short, has not yet grasped the opportunity that the crisis has bestowed on him. It once seemed that, with the liberal economic model apparently undermined, this political opportunity was principally for the left. In Britain's dire fiscal circumstances, it is now clear, it is instead a chance for the right—a chance to revise the dimensions and functions of the state. Yet in public, at least, Mr Cameron is thinking more in terms of penny-pinching efficiencies than about structural reform. For example, he has questioned whether tax credits should extend as far up the income scale as they now do. He should also ask whether other welfare payments, such as child benefit, ought to be paid to the well off. Welfare should become more a safety net and less an indiscriminate bonus. Under Labour the state has acquired new legions of servants, such as the 200,000-odd teaching assistants who have made no discernible difference to exam results. Mr Cameron should ask whether Britain can live without them.

This is not to deny that he has some good ideas (as well as some bad ones, such as his gloomy notion of the "broken society" and his stringent Euroscepticism). But he still seems too wedded to the mild, incremental model of Conservatism that he has long espoused.

Mr Cameron deserves more credit than he sometimes gets for his achievement so far. For a decade before he took over in 2005 his party looked incapable of governing, even when it was still nominally doing it. Now it is set to oust Labour after what will probably be 13 years in office. But to transform Britain for the better after the election—and to earn the support of *The Economist* before it—Mr Cameron must be braver.

On energy, Jimmy Carter, efficiency, Uganda's oil, Asian-Americans, home-schooling, lavatories

Aug 20th 2009
From The Economist print edition

Saving energy

SIR – Your article on Britain's looming electricity crisis touched only briefly on the benefits that stemming the demand for energy could have in preventing the lights from going out ("Dark days ahead", August 8th). Governments must be proactive in demand management. One solution that helps is dynamic pricing, which reduces peak electricity demand by signalling to customers the change in power prices over the course of a day.

In a recent study for America's Federal Energy Regulatory Commission, we estimated that dynamic pricing could lower peak demand by 16% over the next ten years. In Britain, dynamic pricing could be offered once smart meters are rolled out, which the government is already committed to introducing. This would reduce peak demand by about 10GW, equivalent to more than 100 "peaking" power plants of 75MW each, and save several billion pounds in avoided plant costs. With smart-pricing policies, perhaps we can keep the candles in the bottom drawer for at least a few more years.

Ahmad Faruqui
Dan Harris
The Brattle Group
Cambridge, Massachusetts

SIR – Britain's electricity crisis has been caused in part by deregulation, which does not stimulate the construction of new power plants because of the huge capital outlay and attendant risks that are all but impossible to finance. Long-term centralised planning has been ignored, and the greens have stepped into the void. America may well follow suit. I have been in the business for 40 years and I suggest we return to the old model, which produced a reliable service, and put the engineers back in charge.

Jim Mulligan
Binghamton, New York

SIR – You skipped over the effect that emissions-reducing legislation will have in lowering electricity demand. Providing politicians do not waiver in their commitments, the need for heat and power from fossil fuels will fall as a result of energy conservation and efficiency measures.

Indeed, Britain will only meet its target of an 80% reduction in emissions if the demand for energy is curtailed. It will not do so with smoke-and-mirror policies or by manipulating trade figures. Energy companies should not justify increasing their polluting habits with the irresponsible threat of power shortages. They need to do their bit by resisting their desire to build more power plants.

Keith Lodge
Chairman
ECOZEST
Pentrecelyn, Denbighshire

SIR – If Britain does experience severe electricity cuts, do you think the government could save energy by blacking out only the homes and businesses of those who have protested against the building of new power supplies? This should particularly apply to those who do not want wind turbines near their homes, where the reasons for objecting seem to be purely aesthetic.

Robin Conway
Oxford

Presidential reputations

SIR – As an admirer of *The Economist*, I was disappointed to see you compare the effectiveness of Franklin D. Roosevelt with Jimmy Carter, as if they represented two extremes of America's presidency ("Crunch time", August 1st). While FDR may have been the most successful president of the past 75 years in getting his legislation through Congress, Mr Carter actually had a very respectable record. His success rate in getting presidential initiatives through Congress was much higher than that of Dwight Eisenhower, Richard Nixon, Gerald Ford, Ronald Reagan and George Bush senior. In fact, a measure of presidential success compiled since 1953 by *Congressional Quarterly* finds that John Kennedy, Lyndon Johnson, and Jimmy Carter rank the highest in success rates for votes in both chambers of Congress.

Early in his term, Mr Carter clashed with Congress, particularly over water projects he opposed. Furthermore, his congressional liaison staff had problems from the start that resulted in well-publicised complaints, but these were addressed and corrected. Congress supported Jimmy Carter's administration.

Steven Hochman
Assistant to President Carter and director of research
The Carter Centre
Atlanta

The individual in society

SIR – In his defence of economics, Robert Lucas, of the University of Chicago, maintains that: "the term 'efficient'…means that individuals use information in their own private interest. It has nothing to do with socially desirable pricing; people often confuse the two" (Economics focus, August 8th). These two notions of efficiency may be distinct, but the entire justification for a free-market economy is that it should be easy to confuse the two. When the objectives of societies and markets have so clearly diverged, something has gone badly wrong.

Philip Roe
Ann Arbor, Michigan

Distributing oil wealth

SIR – Uganda's oil boom is unlikely to produce much benefit for people living in a country with annual income of $480 per head ("Derricks in the darkness", August 8th). The opaque management of massive oil revenues in oil-rich countries such as Nigeria, Angola and Ecuador has brought little improvement to the lives of their impoverished populations. Moreover, Ugandans have yet to learn details of the deals signed between their government and oil companies. Uganda should commit to a full disclosure of contracts and payments. Foreign oil-companies should then match this promise on transparency and ensure that oil installations and pipelines are developed with the full participation and consent of local communities.

Ian Gary
Senior policy adviser, extractive industries
Oxfam America
Washington, DC

The perils of not being clear

* SIR – Your article on California's Chinese-Americans made the incredible assertion that there are "plans at some university campuses to tighten admissions policies for Asians" ("From nightmare to dream", August 1st). I am surprised that the absurdity of this statement did not give you pause prior to its publication. Do you really believe that, in this day and age, in the United States of America, and in California no less, a university could implement an overtly racially discriminatory policy without inciting a firestorm?

In fact, the campuses in question are tinkering with all admission requirements, reducing the weighting given to standardised test scores. Many Asian-Americans think, perhaps rightly so, that this will result in

fewer Asians being admitted to Californian universities. The point is that you have claimed that a possible consequence of a policy is the actual policy.

David Boettger
San Jose

Home truths

SIR – More parents may be choosing to educate their children at home, but there are many reasons why this is a bad idea ("Kitchen-classroom conservatives", August 8th). Whether or not home-schooled children are academically better or worse than students in public schools is beside the point.

The object of a national education system is not to produce only scholars and workers, but citizens with an understanding of democratic values and a common sense of purpose. It is hard to imagine how the segregation of millions of children, voluntary or otherwise, will not lead to greater polarisation of an already badly divided body politic. When parents keep their children out of public schools, they also lose any influence in reforming the system. Short of living alone in a remote wilderness, barricading oneself from the onslaughts of the world is an ultimately futile enterprise.

Barry Edelson
Huntington, New York

* SIR – The sad truth about home-schooling is that it is selfish, cruel, unchristian, and un-American. Selfish because it is less work, not more, to avoid the challenges of teaching your children to deal with bullying, amorality, and the relentless assault of teachers' leftist propaganda. Cruel because home-schooling denies your children the fullest experience of American life.

Unchristian because Jesus did not turn his back on society. And un-American because religious conservatives who choose to keep their gifted, emotionally stable, morally grounded children out of school are forfeiting the game to the unprincipled left, and in so doing are ignoring the greater need of their country.

Greg Dunn
Bethesda, Maryland

Toilet humour

SIR – Continuing your recent trend for enjoining car superlatives with commodes (Letters, August 15th), may I suggest the "Porsche of potties", the "Jeep of jakes" and the "Hummer of heads".

Peter Shire
New York

* Letter appears online only

Afghanistan

From insurgency to insurrection

Aug 20th 2009 | KABUL
From The Economist print edition

The fraying state of a distant land in which the West seems increasingly bogged down

Eyevine

AT A taxi-rank on the southern edge of Kabul, drivers lounged against dusty car bonnets and held a grim conversation. Business was bad, they said. The road they travelled, shuttling between Afghanistan's capital and the violent eastern provinces of Logar and Paktia, was often unusable. Between 4pm and 4am, Islamist militants preyed upon it. At other times, American troops closed it.

"We're caught in the middle and we're sick of it," said Ghafoor, a resident of Ahmadkhel village in Paktia—where he claimed 60 civilians had been killed in on-off fighting between Americans and militants. "We need security. But the Americans are just making trouble for us. They cannot bring peace, not if they stay for 50 years."

At which, your British correspondent, who had been attracting attention in a dicey area, offered his hand and made to leave. Mr Ghafoor responded with two distastefully outstretched fingers, and said: "I won't shake hands with a Kafir."

It would be wrong to judge any country, let alone one as fractured and complicated as Afghanistan, on an anecdote. Yet this encounter was consistent with a worrying change detected by many grizzled Afghanistan hands, Western diplomats and soldiers. Across Afghanistan, but especially in the mainly-Pushtun south and east (Pushtuns making up about 43% of this multi-ethnic population), resentment against the foreign-funded government of President Hamid Karzai, the NATO-led force that protects it, known as ISAF, and Westerners in general, is growing.

On August 15th a suicide-bomb attack outside ISAF's Kabul headquarters killed seven; on August 18th a salvo of Taliban rockets struck Kabul, including Mr Karzai's palace. The violence was perhaps aimed at Afghanistan's second presidential election, which was held on August 20th amid reports of intimidation and widespread rigging. Yet there are also worrying signs that the Taliban insurgency, now estimated to affect 40% of the country's districts, has in some places become an insurrection.

Eight years after the Taliban were blasted from power by American jets, and despite the splashing of $32 billion of foreign aid on Afghanistan, there are many reasons for Afghan anger. A failure to provide the security they crave—despite the deployment of over 100,000 ISAF and American troops, more than 120 of whom have been killed in the past six weeks—is the most obvious. Almost two-thirds of Afghanistan, one of the world's poorest places, where 30 years of anti-Soviet, then civil and now anti-NATO war have obliterated irrigation systems and turned roads to dust, is considered too dangerous for aid agencies to reach.

Civilian casualties of the fighting, of which there have been over 1,000 this year, are another source of resentment—and another motive for the insurgency in Pushtun society, where vengeance is justice. Nearly 60% of these deaths were in fact caused by the Taliban and allied Pushtun militants, through their increasing use of terrorist tactics, including over 90 suicide-blasts in Afghanistan this year. But misdirected American air strikes, which have many times destroyed wedding-parties and sleeping villagers in Afghanistan—for example, in western Farah province in May when at least 63 civilians were killed—are the main focus for Afghan rage. Acknowledging this, Mr Karzai on the campaign trial has often been critical of foreign troops.

The grudge-list goes on. Afghans, who welcomed this Kafir intervention in 2001 with outstretched arms, tell stories of American and British soldiers barging into cloistered Pushtun women's quarters, at night, with unclean dogs. If often exaggerated, these tales are rooted in truth. Casual detentions of thousands of Afghan men, on no good evidence, have also done damage. In his Kabul home, Abdul Salam Zaeef, the Taliban's black-bearded former ambassador to Pakistan, describes with disbelief the interrogations he endured during three-and-a-half years in Guantánamo Bay. "They said: 'You are Mullah Omar, you are al-Qaeda, you are a drug-dealer, you are a gold-dealer…'"

With too little knowledge and too few troops, America and its allies have often relied on malign local proxies. Underlining the difficulty of the task, many of these held government posts. Between 2002 and 2006 in southern Uruzgan, for example, American special-forces soldiers were persuaded by the controversial then-governor, Jan Mohammad Khan, that a rival Pushtun tribe, the Ghilzais, supported the Taliban. In the mayhem that ensured, this soon became a self-fulfilling prophecy.

Fuel on the fire

Until 2006, southern Helmand had only 300 American combat troops. While thus neglected, it developed into the opium-growing heart of a complicated insurgency in which drugs, tribal politics and Islamist militancy all play a part. The deployment of 3,300 British troops there in early 2006 poured petrol on this fire. Many have been killed—including 35 in July and August—for little obvious gain. An institutional reluctance to admit the obvious—that the British were too few to bring security to Helmand—made matters worse. It led, for example, to an insane tactic of sporadic sweeps by British soldiers through Taliban-controlled areas, known as "mowing the lawn", which might have been designed to turn local villagers to the Taliban. Helmand is now in arms, with 20,000 British and American troops now battling to control its main towns and roads.

Even Lashkar Gah, the provincial capital, is unsafe. Its walls were pasted with a few campaign posters this week, but also with threatening "night-letters" from the Taliban, warning people not to vote. The militants, it was rumoured, meant to cut off the inky forefinger of anyone thus marked as having disobeyed their injunction. A local parliamentarian, Niamatullah Afari, who said he had been unable to visit his lands on the town's outskirts for years, predicted that no Helmandi would vote outside the province's two main towns.

In Helmand, and elsewhere in the south, the illegal opium trade—which the UN estimated to be worth $3.4 billion at export last year, or 33% of GDP—has also been incendiary. British troops in the fertile Helmand river valley, which alone produces more sticky opium resin than any nation, have been unwitting pawns in drug wars involving tribes, government officials and the Taliban, who get perhaps a third of their income from taxing the trade. An American-funded effort to plough up opium poppies, the main cash crop in much of the Pushtun south, has been wasteful and self-defeating. Last year this policy turned Nad Ali, which, under the control of a pro-government drug gang, had been a rare Taliban-resistant district of Helmand, into a place as hostile as any other.

ISAF maps, showing incidents of insurgent violence in yellow, reveal the effect of these setbacks. In 2005 southern and eastern Afghanistan were light yellow, while a speckly yellow arc traversed the west and north. In 2009 Afghanistan is covered by an almost-unbroken yellow ring, encompassing every thickly populated area. The south and east are rich gold. The northern and western arc is now thickly freckled maize. It includes formerly peaceful Kunduz province where German soldiers, sent there by an anxious government largely for their safety, were last month engaged in heavy fighting.

To what extent is the conflict a popular resistance? It is not a national Pushtun insurrection—like those, rooted in implacable xenophobia, that defeated 19th-century British adventurers and Soviet occupiers in the 1980s. By the government's estimate—unreliable as it may be—the Taliban and other Pushtun militant groups may be able to call on 25,000 fighters. Yet there is at least reason to fear, on the evidence of Helmand alone, that foreign troops are now creating more conflict than they can possibly quell. As an

argument for ramping up Afghan security forces—which he later sought to contradict—the Afghan army's spokesman, Major-General Zahir Azimi, acknowledged this. "Where international forces are fighting, people think it is incumbent on them to resist the occupiers and infidels. This feeling is strong in the south and east and it may spread to other places."

Afghanistan, it seems wise to assume, is at a critical point. The news is not all bad. Kabul, recently reinforced by some 4,000 freshly-trained police, feels a bit safer these days. And 21,000 extra American troops, including 17,000 already dispatched to Helmand and elsewhere, could begin to show similar results. Mr Karzai's cabinet has also improved, with half a dozen technocrats recruited in the past year to the main economic ministries. Yet it seems clear that the international effort to bring stability to Afghanistan, in which a strong, somewhat liberal and democratic state can take root, is failing. Among a relatively few foreign experts on the country—as opposed to the thousands of fat-salaried Western consultants bunkered in Kabul—the mood is bleak. "We think we're at the centre of things, but we're not, we're at the margins of Afghanistan," says Martine van Bijlert of the Afghanistan Analysts Network, a think-tank. "And we're so busy having meetings and discussing our plans we're not even seeing what's coming at us." Complete failure—withdrawal by NATO and a return to civil war—seems unimaginable. But failure of some lesser sort, still undefined, looks increasingly inevitable.

Fixing Mad Max

Softening the blow, there are two reasons for hope. First, however angry and disappointed, most Afghans still back the reconstruction effort. A recent poll for the International Republican Institute (IRI) showed them to be optimistic on a range of related issues, including security and the economy. General Stanley McChrystal, the overall American commander in Afghanistan, finds succour in this. Asked whether he considered his mission possible, he said: "Afghanistan is this tremendously complex, Mad Max, utterly devastated society that's got to be repaired, and I don't know if we can fix it. But we can't ignore it. And I believe there are certain forces here, maybe just the will of the people, fatigue with war—there is a tremendous desire to sort it out."

The re-election of Mr Karzai, a clear favourite in this week's vote, would in part be an expression of that desire. A small-time leader in the anti-Soviet *jihad*, from a noble Pushtun family, he was installed as Afghanistan's leader by America in 2001. As a symbol, then, of international support for the country—and not for anything he achieved, while mostly confined for fear of assassination in his Kabul palace—Mr Karzai went on to win Afghanistan's inaugural presidential election in 2004. He has achieved little since, presiding over a spread of narco-corruption by which he seems blithely unperturbed. In July Mr Karzai pardoned five well-connected drug-traffickers who had been imprisoned for up to 18 years for attempting to trade heroin for two truckloads of sub-machineguns. These convictions had been considered a ground-breaking success for Afghan counter-narcotics efforts.

As a hedge against wavering foreign support, Mr Karzai has also favoured detested warlords—including several whom the Taliban were first launched, in the mid-1990s, to eliminate. To boost his chances of re-election, he has formed alliances with Rashid Dostum, an Uzbek warlord linked to the slaughter of 2,000 Taliban prisoners, and Mohammad Mohaqeq, a Hazara strongman, who claims to have been promised five Hazara cabinet seats for his support. As a campaign adviser, Mr Karzai enlisted Abdul Rasul Sayyaf, an Islamist who welcomed Osama bin Laden to Afghanistan in 1996. In an IRI poll released last week, Afghans said that of all their politicians, they disliked Mr Dostum, Mr Mohaqeq and Mr Sayyaf most.

The poll predicted that Mr Karzai would win 44% of the vote—a strong lead over his rivals, but not the outright majority he would need to avoid a second-round run-off, provisionally set for October 1st. At the same time, IRI found that 83% of Afghans thought their country needed to change direction. A surge of support for Mr Karzai's main challenger, Dr Abdullah Abdullah, a champion of the Tajik minority, hints at what sort of change they would like. Unlike Mr Karzai, he has campaigned across the country, rallying Afghans and offering them ideas—some good, some bad—on how to solve their problems. In fact in Afghanistan's main cities, the election has fuelled lively debate, for which Dr Abdullah, and two lesser challengers, Ramazan Bashardost and Ashraf Ghani, deserve credit. Yet even without massive rigging in favour of Mr Karzai—which was expected in Pushtun areas where independent observers will fear to go—he was considered likeliest to win. His reputation, though fading, as a peaceable Pushtun, a national

unifier and, above all, as the likeliest guarantor of the foreigners' shining promise to Afghanistan may best explain this.

AP

They need to be both bolder and more careful

McChrystal's hopes

A second reason for hope is Barack Obama, who on August 17th reiterated his commitment to this war (see article). His administration, the inheritor of a losing cause, has set about turning things around in Afghanistan with vim and humility. The appointment of Richard Holbrooke, who at least has vim, as America's new "Af-Pak" envoy represents an overdue appreciation of the regional dimensions of a conflict in which old rivals, Pakistan and India, Russia and America and Iran, all have a stake. Mr Holbrooke would most like to stop Pakistan suffering—if not abetting—the use of its territory by the Taliban's senior leaders, who are said to reside in the Pakistani city of Quetta. Alas, he has been consumed by the equally pressing task of turning Pakistan against its own Taliban foes, with some success. This week an aide to their leader, Baitullah Mehsud, confirmed that he had been killed in an air strike.

In Afghanistan Mr Obama's arrival has brought a flurry of strategy reviews and a ruthless change of command, to usher in General McChrystal—whose own review will be unveiled later this month. It will re-emphasise that the main goal of ISAF and American troops is to protect Afghans, not kill the Taliban among them. Orders to this effect have already gone out. Air power is to be used only when there is no significant risk of civilian deaths.

In a three-week period last month, an American marine battalion, tasked with taking control of Garmser, a Talibanised district of southern Helmand, called in one air strike, to drop a 500-pound bomb. In the same period in July 2007, British troops in Garmser, albeit facing stiffer opposition, called in air strikes that dropped 12,000-pounds of bombs on the district. On the wall of the marines' base in Garmser, a note reads: "You have to look at these people as if they want to kill you, but you can't treat them that way."

In similar fashion, military convoys are to be driven more carefully. House-searches must be conducted more politely, with respectful understanding of Pushtuns' habit of keeping their womenfolk prisoner and their names secret. Detention facilities, General McChrystal will recommend, should be more humane—and better intelligence gathered from them. Hundreds of civilians are to be sent to assist his forces, mainly to pep up their flagging efforts to provide economic development. Whether ISAF will get more troops, as the general would no doubt like, is unclear. His sacked predecessor, General David McKiernan, requested around 10,000 more American troops—a modest number—and was denied them. Either way, much greater onus will be placed on building up Afghan security forces, a task only seriously begun four years ago. The Afghan army, currently 94,000-strong, is to be pushed to 134,000 within two years. Both it and the Afghan police, of whom there are currently 84,000, may end up being doubled.

The aim of all this is to separate resisters from committed insurgents—to turn the current gold-yellow map back to the lighter hues of 2005. And then to go further. American planners estimate that 70-80% of their enemies should be persuadable, through kinder tactics, economic opportunities—and a formal reconciliation process. That too is on the agenda, though there is currently little agreement on how it might be done. Mr Karzai has often said he is willing to sit down with the Taliban's supremo, Mullah Mohammad Omar. The UN and some European countries would perhaps support that. America, which for seven years has called the Taliban al-Qaeda's cousins, may find this harder to condone. Yet it is worth noting that the Taliban's one-eyed leader has not accepted Mr Karzai's offer.

And why would he? Wherever he is, Mullah Omar must be smiling. America's fresh effort is horribly belated and its commitment to Afghanistan is probably shakier than Mr Obama suggests. To maintain political support for his task, General McChrystal reckons he has a year to show serious progress—a blink-of-an-eye in counter-insurgency time. Nor are all his suggestions entirely new. Previous ISAF commanders, including General McKiernan, also issued promising directives, only to fail because of too few resources and too little understanding in their forces, and too little support from the Afghan government. Rebooting Mr Karzai, assuming that he wins re-election and that it is possible, would be much better for his country than many more American brigades.

But at least Afghanistan's accelerating decline seems at last to have been admitted. That should be a blessing for its people who are caught, wavering, between two enemies. In the words of Colonel Ghooli Khan, the police chief of Garmser, "They do not like the British or the Americans. They just want peace."

American opinions on Afghanistan

A war of necessity?

Aug 20th 2009 | WASHINGTON, DC
From The Economist print edition

Americans are giving Barack Obama the benefit of the doubt. For now

AP

THE orator-in-chief has not lost his touch. Addressing a crowd of military veterans on August 17th, Barack Obama thanked them for their service and vowed to give their successors in uniform everything they might need, while also cutting waste from the military budget. He reminded them that he was cancelling plans for a costly presidential helicopter that, among other things, would have let him cook a meal while under nuclear attack. If America is under nuclear attack, he assured them, "the last thing on my mind will be whipping up a snack".

The main purpose of his speech, however, was to drum up support for the war in Afghanistan. "This is not a war of choice," he said. "This is a war of necessity. Those who attacked America on 9/11 are plotting to do so again. If left unchecked, the Taliban insurgency will mean an even larger safe haven from which al-Qaeda would plot to kill more Americans. So this is not only a war worth fighting. This is fundamental to the defence of our people."

This echoes what Mr Obama said on the campaign trail last year. He made a distinction between the "dumb war" in Iraq and the good one in Afghanistan. Osama bin Laden plotted the toppling of the twin towers from Afghanistan. Overthrowing the Taliban regime that sheltered him was the right thing to do. If elected, Mr Obama promised to pull out of Iraq and concentrate on Afghanistan.

As president, he has kept his word, though not as quickly as he said he would. "We will remove all our troops from Iraq by the end of 2011," he reiterated this week, "and for America, the Iraq war will end." At the same time, he is sending more troops to Afghanistan. Their mission, he says, is to "disrupt, dismantle and defeat al-Qaeda and its extremist allies".

Like George Bush before him, Mr Obama reckons that the best way to sell a war to Americans is to mention al-Qaeda early and often. But also like Mr Bush, his war is more complicated than he makes it sound. American troops are not really fighting al-Qaeda in Afghanistan, because they are not there any more. The group's surviving leaders have mostly fled to neighbouring Pakistan.

They could come back, perhaps, if America were to abandon Afghanistan and the Taliban took over again. Denying them a safe haven is obviously in America's national interest. But there are several other wild places where al-Qaeda might also set up shop, such as Yemen, Somalia, Eritrea, Sudan, the Philippines or Uzbekistan. "We clearly cannot afford to wage protracted warfare with multiple brigades of American ground forces simply to deny al-Qaeda access to every possible safe haven. We would run out of brigades long before bin Laden ran out of prospective sanctuaries," writes Stephen Biddle of the Council on Foreign Relations, a think-tank.

Mr Obama knows this, of course. His purpose in committing so many troops to Afghanistan is not merely to prevent al-Qaeda from returning but also to prevent the country from collapsing into chaos and destabilising its nuclear-armed neighbour, Pakistan. That is too complicated to put on a bumper sticker, but Mr Obama still has the political capital to attempt it.

That may sound surprising. Opinion polls in America show a growing pessimism about Afghanistan (see table). But such gloomy views are seldom offered unprompted. The anti-war movement has all but lapsed into silence. A Democratic pollster asked people at Netroots Nation, a big conference this month for left-wing activists, which issue they were spending most time campaigning about. The war in Afghanistan came last. Like other Americans, progressives are now much more worked up about domestic issues, such as whether they will have health insurance next year. As an electoral issue, Afghanistan is "about as

inconsequential as it could be," says Charlie Cook, a political analyst.

That means that Mr Obama has a relatively free hand in deciding how to deal with Afghanistan, at least for now. Since he did not start the war, no one accuses him of being a warmonger. Since he is prosecuting it seriously, hardly anyone accuses him of being weak-kneed. He has funds, forces and a strategy: to combine rigorous counter-insurgency with efforts to promote development and good governance. He has some time to make it work. But how much?

Gloomy, but not regretful

% replying*

Would you say the US is winning the war in Afghanistan?	
Yes	18
No	42
Not sure	40
Do you favour increasing the number of troops?	
Favour	32
Oppose	41
Not sure	27
What do you think will eventually happen?	
The United States will win the war	35
The United States will withdraw without winning	65
Do you think the United States made a mistake sending troops to fight in Afghanistan?	
Yes	31
No	49
Not sure	20

Source: *The Economist*/YouGov *Poll Aug 16th-18th 2009

Voters may not be paying much attention to Afghanistan right now, but Congress is growing increasingly uneasy, says Jessica Mathews, the president of the Carnegie Endowment for International Peace, a think-tank. Lawmakers worry that the costs of America's huge and open-ended commitment may outweigh its benefits. Counter-insurgency campaigns typically take many years, cost a fortune in blood and treasure and end in failure. The people who know most about Afghanistan are often the gloomiest. "Is Nation-Building Doomed?" asks *Foreign Affairs*. "Is It Worth It?" wonders the *American Interest*.

Mr Biddle, who wrote the article in the *American Interest*, thinks the war is worth fighting, but only barely. The costs will be high, the outcome uncertain. Mr Obama's strategy promises more bloodshed in the short run in exchange for a chance of stability in the long term. That is hardly a combination that will appeal to voters, so it will be hard to sustain political support for it for long enough to make it work.

If the number of American deaths rises too fast, Americans will start to take notice of Afghanistan and Mr Obama's job will become much harder. Mr Cook cautions that the body count would have to rise very sharply indeed to affect the mid-term congressional elections next year. But that is not impossible. The war "will not be quick", warned Mr Obama this week, "nor easy". Ms Mathews goes further: Afghanistan could be for Mr Obama what Iraq was for Mr Bush, or even what Vietnam was for Lyndon Johnson.

Health reform

The labours of Sisyphus

Aug 20th 2009 | NEW YORK
From The Economist print edition

Opposition to health-care reform is mounting. Barack Obama must now decide whether to scale back his approach

Illustration by David Simonds

DO THE Republicans scent blood? One sign that they might came this week, in the form of a sharp letter from John Boehner, leader of the Republicans in the House of Representatives, to the head of the Pharmaceutical Research and Manufacturers of America (PhRMA) lobby—long a good friend to the party. Mr Boehner denounced as "appeasement" the lobby's decision to support Barack Obama's plans for health-care reform. But that decision was made months ago; attacking it now is surely a sign that the Republicans think Mr Obama is suddenly in trouble.

And with some justification. First, the Democrats failed to meet the president's deadline for getting health bills out of both the House and the Senate by August. Next, as politicians headed home to conduct town-hall meetings during this month's recess, they encountered many constituents angry about the dangers—real or imagined—to be wrought by health reform. Some of these grumblers were planted by conservative groups, but many others were genuinely afraid or upset.

A new poll conducted for *The Economist* by YouGov confirms that scepticism over the reform effort is widespread. Of those respondents expressing a clear view, twice as many believe reform on the scale Mr Obama is still contemplating will leave them worse off than today (38%) as believe they will be better off (19%). Over half are convinced they will end up paying more. And more people (59%) believe that any new system will lead to rationing of care than think it will lead to long-term cost savings (only 46%). Details are available at www.economist.com/yougovpoll.

So will health reform prove to be Mr Obama's Waterloo, as Jim DeMint, a Republican senator, claimed recently? Not necessarily. Michael Cannon of the Cato Institute, a think-tank, opposes Mr Obama's health proposals but believes it is still early days. The real battle is to come in the autumn session of Congress, beginning on September 8th. And the hornets' nest of trouble stirred up by opponents of reform will not soon be forgotten.

This suggests that Mr Obama now faces a difficult choice. One option is to stick with his plans to tackle all the big problems of health at once, ranging from cost to coverage to quality. Another option is to scale back his ambitions, going for the less grand but still worthy goal of expanding health cover to the many tens of millions without it. A third option, giving up altogether, seems unlikely, since Democrats have big majorities in both houses of Congress (though it is possible that in-fighting among Mr Obama's allies could yet scupper even modest reforms).

Officially, the White House is sticking with its original plan for comprehensive reform this year. Look closer, though, and it becomes clear that Mr Obama is signalling that he may soon backpedal in various ways. One example is the rebranding of health-care reform as "health-insurance reform", a carefully worded phrase now repeated by all his officials. This might allow the administration quietly to back away from its "Big Bang" approach, and to claim victory if a timid health compromise manages only to improve coverage while largely ignoring questions of cost and quality.

Another example of back-pedalling is Mr Obama's wavering support for a government-run health-insurance plan. Though this notion is wildly popular with the political left, conservatives and business lobbies loathe it. Concerned that moderate Democrats may vote against any final health bill containing such a controversial public plan, the administration this week softened its support for the notion. Mr Obama still advocates the idea, his aides insist, but is willing to live without it if that is the cost of a health deal.

Predictably, many liberals are outraged by any talk of weakening reforms. Robert Reich, a labour secretary under Bill Clinton, this week declared that leftists must march in support of the public plan in Washington, DC, on September 13th. Polls show support from Democrats plunging if no public plan is included.

If reform were to be scaled back, would that be a disaster? The loss of a public-plan option need not be. One reason is that support is growing for non-profit "co-ops" instead of a government-run plan to compete against private insurers—though it looks as though the Republicans are gearing up to attack these, too. A bigger reason is that pioneering reformers in Europe and in Massachusetts have shown that universal coverage is achievable without a government-run insurer. Among the policies needed are strong regulation of insurers to prevent bad behaviour, subsidies for the poor and the creation of health-insurance exchanges.

But surely going only for coverage now just delays the task of cost control until later? Yes, but that is a good thing, argues Jon Kingsdale. As head of the Commonwealth Connector, the official insurance exchange set up in Massachusetts, he has seen at first hand how the raucous politics of reform have unfolded in his state. Michael Dukakis, a former governor, tried to fix health care 20 years ago, but the law he pushed through the legislature eventually came undone in the teeth of business opposition. The new reforms, passed three years ago, have cut the number of uninsured in half, so that only 2.6% of people in the state are now without insurance.

Hasn't this politically attractive entitlement simply made the cost problem worse? After all, many economists argue that national health reforms must tackle costs hand-in-hand with coverage or else be deemed reckless. On the contrary, says Mr Kingsdale, sequencing reforms slowly and building support through expansion of coverage has now made it politically feasible for his state to tackle the cost problem. The key, he insists, is to see reform not as a Big Bang but a continuing process.

To bolster his contrarian argument, he points out that an officially appointed committee of experts has just recommended that his state scrap the fee-for-service model of reimbursement, which many economists believe is at the heart of America's health-inflation problem. Doing so would require his state to get a special waiver from the federal government, but this radical and hugely worthwhile proposal is now being seriously considered. Sadly, the idea is nowhere to be found in the leading bills in Washington, DC.

Mr Kingsdale does acknowledge that it is easier to pull off reform in a small and wealthy state like his than it would be at the national level, and accepts that his state has not yet actually passed any legislation that would curb health inflation. And given Congress's history of fiscal irresponsibility, it is surely right to be sceptical about any strategy that expands entitlements today in the hope of forcing a fiscal crisis to win support for cost cuts tomorrow.

Mr Kingsdale sums it up this way: "Trying to anticipate and address related cost, quality and access issues in one national reform would be more than Herculean—it would be Sisyphean…Herculean effort, followed by failure, then a renewed attempt at reform, ad infinitum." Sadly, that infernal tableau describes all too

well the fate of most health reforms attempted since the days of Theodore Roosevelt. Lyndon Johnson was the only exception. Can Mr Obama provide another one?

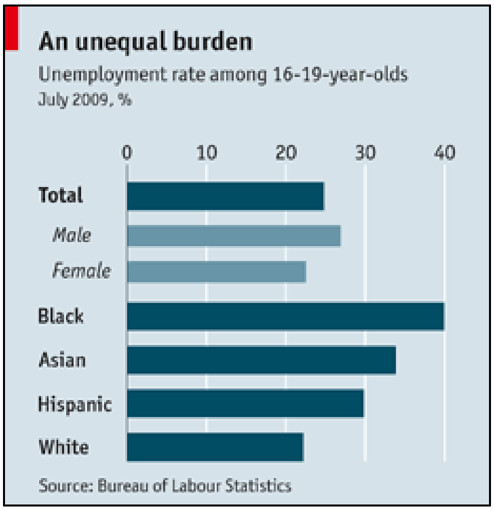
Dick Armey, a former majority leader of the House, discusses opposition to health-care reform here.

Youth unemployment

Left behind

Aug 20th 2009 | WASHINGTON, DC
From The Economist print edition

The recession may have a lasting effect on young people



AMERICA'S capital enrolled some 20,000 youth in a jobs programme this summer, part of a national effort to get young people to work. Some spent the summer in the offices of Adrian Fenty, Washington's mayor. Others joined a "conservation corps". Delonte Brown, 16 years old, spent nine weeks at Powell House, a non-profit organisation, learning about the arts industry and acquiring various job skills while earning an hourly wage. Now the summer is ending. Mr Brown is one of the lucky few in a jobs programme during the school year too. For most, work will vanish with the summer. In July the national employment-population (E/P) ratio was 59.4%. For teenagers it was 28.9%, the lowest on record.

Young people always have lower levels of employment. They may forsake work to focus on their studies, hardly a bad thing, or be willing to wait for the right job. But they are also less experienced job hunters, less mobile, less skilled and often the first to be fired. Since 2000 they have had an especially hard time, explains Andrew Sum of Northeastern University's Centre for Labour Market Studies (CLMS). One possible reason is that the old are elbowing out the young. The teenage E/P ratio dropped by 34% between 2000 and 2008. It rose by 7% for those aged 55-64 and by 29% for those aged 65 and older.

All types of young people have suffered. In the first quarter of 2009 only half of young college graduates had jobs that matched their education, according to CLMS. Figures are worse, however, for those who are teenagers, male, poor or black. Those with a combination of these traits have particularly glum statistics. The E/P ratio for poor black teenagers was only 12% in the first quarter of the year. Middle- and upper-class whites and Hispanics were three times as likely to be working.

The stimulus bill, passed in February, included $1.2 billion to help find jobs for those aged 14-24. The White House encouraged much of the money to be spent this summer, through programmes that subsidise jobs in the public and private sector. Hilda Solis, the labour secretary, is a firm believer in summer jobs programmes—not least because she took part in one as a teenager. The administration estimates that the stimulus will put 200,000 young people to work this summer. The push helps, but not enough.

The main federal effort to help the young, the Workforce Investment Act (WIA), has historically failed to reach many of the 3.5m-5m young people who are neither in school nor working. Washington, DC, offers an example of a local programme with good intentions, high costs and limited efficacy. This summer's $23m budget had to be almost doubled. Despite some heartening evidence, it is unclear that the programme reaches those most in need of help or provides the skills needed to get a job in future. But since the city has yet to spend its stimulus allocation, it could opt for a year-round effort to target the most isolated teenagers. Linda Harris of the Centre for Law and Social Policy, which lobbies for the poor, wants a broad overhaul of WIA—the law has been due for reauthorisation for years.

Meanwhile, the labour market remains dismal. Complicating the matter, the federal minimum wage rose last month, which may further depress the employment prospects of young, unskilled workers. And as the recession drags on, ever more youngsters are likely to find themselves left in economic limbo. Young people with jobs are more likely to graduate from high school and earn higher wages as adults. So lack of employment now may portend an even bleaker future.

Drinking laws

The 21 Club

Aug 20th 2009 | NEW YORK
From The Economist print edition

Underage drinking and deaths have prompted a movement for change

NEARLY 5,000 people below the age of 21 die because of excessive alcohol consumption each year. Oddly, this has triggered a new movement to lower the drinking age. In America, young people can vote, drive, marry, divorce, hunt and go to war before alcohol is legally allowed to touch their lips. Many states once set their minimum drinking-age at 18. But in 1984 Ronald Reagan oversaw the passage of the "21 law", which requires states to set 21 as the minimum drinking-age or risk losing 10% of their highway funds. Now campaigners want to move it back.

In the past, states have been too fiscally timid to challenge the 21 law. But calls for change are growing louder. Two local magistrates in South Carolina recently ruled that banning 18- to 20-year-olds from drinking or possessing alcohol is unconstitutional. Public officials, including the former attorney general of South Dakota, have called the 21 law a failure. The about-face of Morris Chafetz, a doctor who served on the commission that recommended increasing the drinking-age to 21, has also raised eyebrows. This week he called it the most regrettable decision of his career.

Supporters of the status quo, including the organisation Mothers Against Drunk Driving, say that the law has averted thousands of fatalities. But sceptics point out that other countries, like Canada, have seen similar declines, even though their drinking-age is 18. They also argue that barring young people from drinking does not stop them from consuming alcohol: it just makes them drink more quickly.

John McCardell, former president of Middlebury College in Vermont, is part of the Amethyst Initiative, a group of educators who are pushing for 18-year-olds to be allowed to drink. Those who have graduated from high school, have a clean record and completed an alcohol-education programme should qualify for a drinking licence, he says, in the same way that people who go to driving school receive a licence to operate a vehicle.

This is not the first time that Americans have hankered for a change in alcohol policy during a period of economic distress. Franklin Roosevelt repealed prohibition in 1933 amid the throes of a depression. "I think this would be a good time for a beer," Mr Roosevelt said, before signing the 21st amendment.

The worst unemployment figures

Benefits and the border

Aug 20th 2009 | EL CENTRO, CALIFORNIA
From The Economist print edition

A simple but awkward explanation for the highest jobless rate in America

THE small city of El Centro, "the centre" in Spanish, is the centre of nothing obvious except an unforgiving desert. It is, rather, at the very edge of America, blending into Calexico, the border town that leads to the much larger Mexican industrial city of Mexicali. But El Centro has been receiving unusual amounts of attention because it is the metropolitan area that has America's worst unemployment—at 27.5%, as of June, almost three times the then national rate of 9.7%.

"We're not disputing the numbers, but there are numbers missing," says Ruben Duran, the city manager, or equivalent of mayor. He has tolerated with good humour a steady influx of journalists determined to declare El Centro the "centre of the Great Recession". Whatever it is, it is not that.

The locals admit that El Centro—and indeed all of Imperial County, of which it is the seat—is rather a boring place. In the winter there is fun to be had by racing over the nearby sand dunes in four-wheel-drive buggies. In the summer though, when the heat reaches 45°C (113°F) degrees and metal door knobs are scalding on the outside, the streets are empty as families spend air-conditioned time indoors. But despite the gloomy figures, the place is far from squalid. There are several well-attended Starbucks outlets, and a four-year-old mall does brisk business.

El Centro's employment is dominated by federal, state and local government, in particular two nearby prisons and the ubiquitous Border Patrol, all relatively untouched by recession. The housing bust has destroyed some jobs in construction, but that is true of many places.

Fluctuations in the job market tend to be seasonal rather than cyclical because of the agricultural calendar, a point that Mr Duran illustrates with his favourite research toy, Google Earth. Zooming out from El Centro, he shows green rectangles in the white desert where lettuce, carrots and a few other crops are grown with water tapped from the Colorado river and brought in through the All-American Canal along the Mexican border (the scarce groundwater is brackish).

Every winter, between November and March, El Centro bursts into activity as pickers work 12 hours a day to harvest lettuce for $8-10 an hour. The unemployment rate drops by a few percentage points. Then, in March, the harvest moves north to places such as Salinas. In the old days the pickers migrated, but these days they stay and collect unemployment benefits during the summer months.

Seasonal variations, however, are common to all farming areas. They don't explain a stubborn "baseline" unemployment of about 12% that never goes away, says Mr Duran. He zooms out further in Google Earth to display the single vast conurbation that is El Centro, Calexico and Mexicali, with one tentacle reaching toward Yuma, Arizona, which, at 23.1%, happens to have the second-highest unemployment rate in America after El Centro. Here is the answer, he says, pointing at the map.

El Centro is about 70% Hispanic, and Spanish is the dominant language on the radio and streets. But illegal immigrants from Mexico tend to move through Imperial County and beyond it. The Latinos who remain are mostly dual citizens or green-card holders, who go back and forth across the border with relative ease.

Many families live in both places, and many Mexicali mothers carpool to drive their children across the border to schools in El Centro, then recharge at Starbucks and Macy's before driving back to Mexico. A lot of the cars parked at the mall have Mexican licence-plates. Timothy Kelly, the boss of the Imperial Valley

Economic Development Corporation, estimates there are also some 40,000 to 60,000 people who live in Mexicali but work in El Centro.

By the same token, there must be people who live in El Centro, at least officially, and work in Mexicali making windscreens and refrigerators. Many of them might nonetheless collect unemployment benefit in El Centro at the same time. “If we added the Mexicali jobs, then we would have a normal unemployment rate,” argues Mr Duran.

This explanation seems anecdotally plausible. Francisca German, a manager at One Stop, an agency that tries to help people find jobs, says that, of the 3,000 people or so who come through her door every month, many are “not motivated” to find jobs, but just need proof that they tried. Others, of course, make a genuine effort.

Mr Kelly in El Centro, meanwhile, does not intend to imply that unemployment fraud explains all of El Centro’s problems. Many of its people lack the education and proficiency in English for modern jobs. But Imperial Valley does shows great promise for the green economy. Two companies have set up shop to harvest geothermal energy—photoelectric energy will surely be another runner as the technology improves—and Mr Kelly is inviting others. Biomass projects, involving growing algae on nearby lakes, are another option under consideration. El Centro is likely to stay what it is: neither forsaken nor bustling, but simply on the border.

Gay-marriage laws

Still waiting

Aug 20th 2009 | WASHINGTON, DC
From The Economist print edition

The White House still opposes the Defence of Marriage Act

BARACK OBAMA tends to become incoherent when discussing gay rights. During the campaign he said he supported equal rights for gays but also that marriage should be "between a man and a woman". He opposed both same-sex marriages and a law that bars them, California's Proposition 8. He favoured repealing both "Don't Ask, Don't Tell", which keeps gays from serving openly in the armed forces, and the Defence of Marriage Act (DOMA), which created a federal definition of marriage. As president, however, he has done little. At a White House reception for gays in June, the most notable event was that a mobile phone started quacking. Gays might be excused for thinking their president was doing the same.

It is not surprising that gay rights are a relatively low priority. In 1993 uproar over gays in the armed forces buried Bill Clinton's early agenda. Mr Obama's problems already include a recession, two wars, unwieldy bills and citizens warning his congressional allies of judgment day.

But a lawsuit over DOMA has put Mr Obama in a bind. The law, passed in 1996, lets the federal government ignore same-sex marriages (denying partners benefits, for instance) and allows states to ignore those licensed elsewhere. Now a married gay couple is challenging the law in court. The Justice Department usually defends acts of Congress, regardless of the president's position. So a brief it filed in June was bound to enrage. The department claimed that DOMA does not discriminate, despite granting federal benefits only to straight couples, and that if states can ignore a marriage between an uncle and niece, they can ignore gay marriages too. Joe Solmonese of the Human Rights Campaign, an advocacy group, wrote: "I hold this administration to a higher standard than this brief."

A moment of clarity came on August 17th. Though the Justice Department continues to defend DOMA in court, it stated that the administration believes the law "is discriminatory, and supports its repeal." The brief also rejected claims that the government has an interest in preventing gay marriage, writing that children raised by gay couples are as likely to be well adjusted as those raised by heterosexuals.

Advocates reacted cautiously. "It might seem obvious that denying same-sex married couples all the federal protections that other married couples get is discrimination," said Matt Coles of the American Civil Liberties Union. "But having the federal government finally admit it is a promising sign." Mr Obama may proceed in small steps. After the uproar over June's brief he extended some benefits to same-sex partners of federal workers. Meanwhile, states are being bolder—Iowa, Vermont, Maine and New Hampshire have each authorised gay marriages within the past five months. Those hoping for action in Washington may have to wait until the White House quacker is a lame duck in 2013.

Robert Novak

The prince of darkness

Aug 20th 2009
From The Economist print edition

Farewell to one of Washington's great insiders

Getty Images

The prince in his pomp

BOB NOVAK, who died on August 18th, was a Washington institution for more than 50 years. His column, which was syndicated in almost 300 newspapers and appeared as often as six times a week, was compulsory reading for anybody with even a passing interest in politics. He was also a fixture on the political talk shows, with his trademark three-piece suit and arched eyebrows, and his mouth always ready to break into a sneer.

Mr Novak's great claim to fame was that every column that he wrote included some breaking news. Rival reporters wondered whether there was a law which forced politicians to talk to him. But his unrivalled access was actually the result of a combination of hard work and hardball. He had the requisite friends in high places—LBJ even hosted a reception for his wedding—but those friends also found their tongues loosened by the knowledge that you were either "a source or a target".

Mr Novak's brand of insider journalism frequently put him at the centre of the political storm. His assertion that a leading Democrat had told him that George McGovern stood for "amnesty, abortion and acid" exacerbated divisions within the Democratic Party and provided the Republicans with an ideal slogan. His decision to out Valerie Plame as a CIA agent led to one of the nastiest scandals of the second Bush presidency, with Judith Miller, a fellow journalist, spending time behind bars and Scooter Libby, Dick Cheney's chief of staff, being forced to fall on his sword. Mr Novak's critics regarded him as "the prince of darkness", a nickname he liked so much that he used it as the title of his autobiography.

Mr Novak had nothing in common with the partisan water-carriers who pass themselves off as conservative "journalists". He described George Bush's presidency as a failure. His fierce opposition to the Iraq war led David Frum, a leading neoconservative, to denounce him as unpatriotic.

The Plame affair led some to dismiss him as a political tool, a criticism with some substance. But political journalism inevitably involves trade-offs between gaining access and rewarding your sources. These trade-offs allowed Mr Novak to provide his readers, for decades, with glimpses into the darkest corners of American political life.

Statewatch: Maryland

Thanks be to DC

Aug 20th 2009 | BALTIMORE
From The Economist print edition

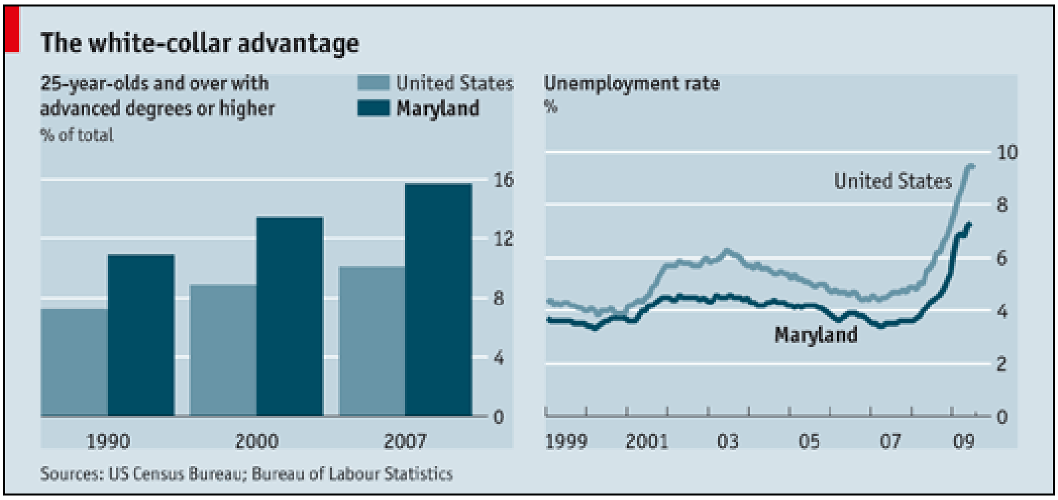
The benefits of proximity to big (and getting bigger) government

FANS of "The Wire", a television series set in Baltimore, will recall a scene in which Omar, a shotgun-wielding stickup artist, strides through an alley clad in a satin blue kimono in a futile effort to find his favourite breakfast cereal. The houses surrounding that alley are among 900 in east Baltimore razed or about to be razed to make way for a $1.5 billion, 87-acre (35-hectare) development centred around a new office park designed to attract start-up life-science corporations eager to be close to Johns Hopkins University. The university gets more money in grants from the National Institutes of Health than any other institution in America and is Maryland's largest private employer.

Less than half of those houses were occupied. The area just outside the development can feel like a film set, with all the elements of urban life—houses, traffic lights, streets, a few cars—in place, except for the people. Baltimore's population has fallen from around 950,000 in 1950 to around 637,000 today; vacant houses dot the city's rougher districts.

Many of Baltimore's economic problems, however (the decline of the shipping and steel industries, a falling population) predate the current recession; and Maryland's largest city is actually faring relatively well today. The area's unemployment rate of 7.4% in the first three months of this year was lower than the national average of 9.5%, and its gross metropolitan product (GMP) fell 2.6% from its pre-recession peak, compared with a national average GMP decline of 3.3%.

These numbers echo Maryland's, which has an unemployment rate of 7.3%. It has America's second-highest median income, and one of the highest percentages of workers with advanced degrees (15.7%). In June 2008 Martin O'Malley, Maryland's governor, unveiled the BIO 2020 Initiative, America's largest per-capita state investment in biotech, comprising some $1.1 billion over the next ten years in tax credits and state venture-capital funds.



The state's biotech industry is concentrated along the interstate highway running between Frederick—home to Fort Detrick, an army base that hosts much of the federal government's biological research capacity—to Washington, DC. In Maryland, most roads lead to Washington. Around 5% of its workers are employed by the federal government; many others work for companies that thrive due to their proximity to Leviathan. The state houses 50 federal agencies, with tendrils of others extending into Maryland as well.

The Environmental Protection Agency, for instance, is headquartered in Washington, but its laboratory-

heavy Environmental Science Centre is located at Fort Meade, an army base in Anne Arundel county some 25 miles from Washington. Fort Meade houses 86 military and governmental entities, it is the state's largest employer, and contributes roughly $4 billion a year to Maryland's economy.

Nearly 40,000 people work at the base, many of them civilians, and a reorganisation of military infrastructure ordered in 2005 is expected to bring another 22,000 jobs to the area. A 36-hole golf course has given way to a huge complex for the Defence Information Services Agency—the IT department for the armed forces. The base's largest tenant is the National Security Agency (pictured), which accounts for over 50% of Fort Meade's workforce.

Corbis

Of course, there is another Maryland, distant from the federal government. Before the summer, unemployment in six of the nine counties east of the Chesapeake Bay topped 8%, while central Maryland's ranges from just below 5% to just over 6%. The state is due to get around $4 billion in stimulus money: most will go to health and education.

The ailing blue-crab industry, meanwhile, based in eastern Maryland, will receive a paltry $10m. The Chesapeake Bay cuts the state's eastern part almost entirely off from mainland America. For centuries this "immense protein factory", as the bay was called by H.L. Mencken, Baltimore's renowned literary son, kept most of America's east coast in crabs, oysters and rockfish.

This year, however, the Phillips picking house on Hooper's Island is still closed halfway into crab season for the first time since 1917. It is not alone. Crab-picking was long the province of watermen's wives; in recent years Mexicans have been brought over to fill the gaps, and this year tough new visa caps have kept the guest workers away. This comes after years of decline due to crab imported from South-East Asia. And its closure has affected eastern shore industries of all sorts, from suppliers of cardboard boxes to the picking houses to coolant salesmen, whose product is not needed when refrigerators are bare.

Economist.com
WORLD
UNITED STATES

Lexington

Still crazy after all these years

Aug 20th 2009
From The Economist print edition

The perils of losing one's grip on reality

Illustration by KAL

NOT long after the assassination of John Kennedy in 1963, the Senate contemplated a bill to tighten federal control over the sale of guns through the post. Three gun-lovers drove 2,500 miles from Arizona to Washington, DC, to protest. One argued that the bill was part of "a further attempt by a subversive power to make us part of one world socialistic government" and that it could "create chaos" and help "our enemies" to seize power. Not much has changed since Richard Hofstadter described this incident in a hugely influential book, "The Paranoid Style in American Politics". Gun-lovers still argue that the slightest curb on their right to bear arms will make America vulnerable to tyranny. And in other areas, too, the paranoid style is alive and frothing.

Some of Barack Obama's detractors content themselves with arguing that he is a bad president. Others go further. "Birthers" insist that he was not born in the United States and is therefore constitutionally barred from being president. Yet Mr Obama's birth certificate says he was born in Hawaii, and there is not a shred of evidence to the contrary. There is even an announcement of his birth in the archive of the *Honolulu Advertiser*, a local newspaper. Yet the internet crackles with theories as to how all this was faked so that, 48 years later, Mr Obama could impose a socialist state on America. And a YouGov poll for *The Economist* found that 26% of Republicans think Mr Obama is probably foreign-born.

Other conspiracy theories about Mr Obama are even loopier. For example, some Americans think he is the Antichrist. The evidence for this, apparently, is that in the Bible Jesus is quoted as predicting that Satan will come down like lightning from heaven, and the words for "lightning" and "heaven" in Hebrew sound a bit like "Barack Obama". Plus, his presidential limo is nicknamed "The Beast". For those who think this is too far-fetched, there is the theory that Mr Obama is a closet Nazi. He thinks abortion should be legal. Historically, some abortion advocates have also been eugenicists. Therefore he must be one of them. Also, he wants to discourage smoking. So did Hitler!

Hofstadter, writing at the time of Barry Goldwater's insurgency, argued that political paranoia—a mix of anger, heated exaggeration, suspiciousness and conspiratorial fantasy—was most evident on the extreme right. And there are plenty of examples of right-wingers peddling nutty tales. Isolationists in the 1940s accused Franklin Roosevelt of deliberately letting the Japanese bomb Pearl Harbour to provide an excuse for war. Talk-radio crackpots in the 1990s accused the Clintons of having Vince Foster, a depressive friend of theirs who killed himself, murdered.

But the left is hardly immune to such fantasies. Some people, including Mr Obama's own former pastor, Jeremiah Wright, believe that AIDS was cooked up by the government to kill blacks. A staggering 18% of Americans think that the government of George Bush probably knew in advance about the attacks of September 11th 2001 but allowed them to proceed anyway. Some even contend that Mr Bush orchestrated the attacks himself, to create an excuse for invading Iraq. To believe this, you have to believe that the Bushies were both wicked enough to murder thousands of Americans and brilliant enough to execute such a mind-bogglingly sophisticated plot without a single leak—in a culture where Richard Nixon could not even hush up a burglary.

Belief in conspiracy theories can be comforting. If everything that goes wrong is the fault of a secret cabal, that relieves you of the tedious necessity of trying to understand how a complex world really works. And you can feel smug that you are smart enough to "see through" the official version of events. But widespread paranoia has drawbacks. For a start, it makes calm, rational debate rather tricky. How can you discuss the trade-offs of health-care reform, for example, with someone who thinks the government is plotting to kill grandma? It does not help, either, that politicians on both sides are willing to fan the flames. Sarah Palin calls Mr Obama's health-care proposals "evil". Harry Reid, the Senate majority leader, calls the protesters who loudly oppose them "evil-mongers". Nancy Pelosi, the speaker of the House of Representatives, calls them "un-American".

It's serious

In his book "Voodoo Histories: The Role of the Conspiracy Theory in Shaping Modern History", David Aaronovitch argues that conspiratorial fantasy can have dangerous real-world consequences. Hitler read and believed The Protocols of the Elders of Zion, a bogus account of a global Jewish conspiracy. So did the founders of Hamas. Timothy McVeigh killed 168 people with a bomb in Oklahoma in 1995 because he thought the federal government was hatching various dastardly plots.

Some people watch the ferment at town-hall meetings in America today and worry that another Oklahoma-style atrocity is brewing. A few protesters are waving placards wishing for Mr Obama's death. Others are ostentatiously wearing firearms outside his rallies. A recent report by the Southern Poverty Law Centre describes an uptick in the number of "Patriot" militia groups since Mr Obama's election and frets that some could turn violent.

One should not exaggerate such threats. The Secret Service does not let gun-wielding protesters too near the president. And the vast majority of people who visit crazy websites will never hurt anyone. But there is no cause for complacency, either. Politicians should tone down the rhetoric. Protesters should read some history before making Hitler comparisons. Talk-show hosts should stop pretending that paranoid nitwits are asking reasonable questions. If people are continually told that their government is plotting against them, a few may decide to fight back. And as Lee Harvey Oswald showed, even one man with a violent sense of grievance can do a lot of harm.

Economist.com/blogs/lexington

Venezuela's education "reforms"

Hugo Chávez seeks to catch them young

Aug 20th 2009 | CARACAS
From The Economist print edition

A hastily passed education law is part of the president's plan to take control of all aspects of Venezuelan society

Reuters

THE first time Hugo Chávez made a serious attempt to reshape the Venezuelan education system, the resulting political battle contributed to the coup that in 2002 briefly ousted him from the presidency. A new education law, shoved through parliament on the night of August 13th after minimal debate, already has the opposition talking of civil disobedience.

The government claims that the law will overcome centuries of exclusion, at last giving the children of the poor equal access to education. But its critics argue that it fails to deal with the key causes of inequality—low-quality teaching, crumbling buildings and widespread truancy in state schools. Whereas Mr Chávez's Ecuadorean ally, Rafael Correa, seems sincere in his drive to raise educational standards (see next story), the focus of the Venezuelan leader's reforms is on ensuring the intrusion of politics at every level. Mariano Herrera, an educationalist, predicts that the result will be greater inequality, not less.

Teaching is to be rooted in "Bolivarian doctrine", a reference to Mr Chávez's ill-defined Bolivarian revolution—supposedly inspired by Simón Bolívar, a leader of Latin America's 19th-century independence struggle. Schools will come under the supervision of "communal councils", indistinguishable in most places from cells of the ruling socialist party. Central government will run almost everything else, including university entrance and membership of the teaching profession.

Couched in vague terms, the law acquires coherence when seen against the president's professed intention to establish revolutionary hegemony over Venezuelan society. In a 2007 campaign on a referendum on constitutional change, Mr Chávez lectured a bemused public on the writings of Antonio Gramsci, an Italian communist who died in 1937. In essence, Gramsci said that to eliminate the bourgeois state one must seize the institutions that reproduce the dominant class's thought-patterns.

The three most important of these institutions, the president noted, were the church, the education system and the mass media. Among the iniquitous doctrines with which they poisoned the minds of the masses, he argued, were representative democracy, the division of state powers and alternating government.

The new education law also lets the government suspend media outlets that affect the public's "mental health" or cause "terror" among children. It threatens to end subsidies for church-run schools that educate the poor. And it seeks to weaken or abolish students' and teachers' unions and to "democratise" university authorities.

How much of Gramsci the president has actually read is unclear. What is apparent is that the law was not framed in parliament but by a team of ideologues in the presidential palace. Legislators suspect Cuban specialists had a hand in it, along with radicals from the Spanish left in Mr Chávez's close circle.

Whether or not it can be implemented as intended will become clear as schools and universities reopen in September. Some opposition politicians and educationalists want to gather signatures for a referendum to repeal the law, as is allowed under the constitution. Student groups, the church, the media, parents and teachers could together form a powerful coalition.

University rectors say the hasty way the law was passed violated both parliamentary norms and the constitution. They were tear-gassed when they approached parliament as it was being debated, to try to deliver a document criticising its content. But a campaign of peaceful resistance is gathering strength.

Since winning a referendum in February abolishing term limits (thus allowing him to seek re-election again in 2012), Mr Chávez has stepped up the pace of his revolution. He has taken powers and funds from mayors and governors, clamped down on independent trade unions and broadcasters, and passed a law which will allow the government-controlled electoral authority to gerrymander constituency boundaries. A wilting economy and a lack of money to spend on his ambitious welfare programmes have begun to sap Mr Chávez's popularity, forcing him to keep casting around for fresh scapegoats.

In his weekly broadcast on August 16th he promised a stimulus package but gave no indication of how he would pay for it. With public dissent growing, his response has been to stifle sources of independent thinking, be they private television channels, trade unions, the church or the schools and universities. However, once he has achieved complete dominance over them all, there will be no one left to blame for the country's ills but himself.

Ecuador's education reforms

Correa's curriculum

Aug 20th 2009 | QUITO
From The Economist print edition

The president seeks to improve ailing schools and universities

AS IN Venezuela, education reforms in Ecuador, promoted by its left-wing president, Rafael Correa, have led to protests and tear-gas on the streets. The teachers' union and the students' federation, both linked to a Maoist opposition party, are furious at proposals to sack bad teachers and make schools and universities account better for the $2.3 billion or so a year the government spends on them.

Ecuador's schools are poor even by South America's generally low standards. Although almost all of its children enroll in primary education, fewer than two-thirds make it to secondary school. By 2015 Mr Correa, a former economics professor re-elected for a second term in April, wants state schools to match the quality of elite private ones like the Lycée La Condamine in Quito, which his own children attend.

Mr Correa is going about his reforms more sensibly than his Venezuelan chum, Hugo Chávez. Awash with oil revenues because of strong crude prices, he has, since coming to office in January 2007, spent around $280m repairing schools and building new ones. In impoverished places like Zumbahua, a remote village in the Andes where Mr Correa once did voluntary work, high-tech "schools of the millennium" have risen among the maize and potato fields. Some of the cheapest private schools have already closed as state schools have scrapped fees and started providing meals for pupils, says Verónica Benavides, a senior education official.

But it is not just about spending more money. Mr Correa wants to supervise more closely how the education budget is spent, and to improve the quality and consistency of teaching. At present, schools have so much leeway that comparisons between the wide variety of leaving certificates they issue are all but meaningless. The government is seeking to impose a standard, minimum syllabus.

Early in his first term, applicants for teaching jobs were set a voluntary test of reading proficiency and logic. Just 4% of those taking the logic test passed it. The government is now making tests compulsory for existing teachers. Those who flunk them will be offered a year's training and then be required to resit them. Those who fail a second time face the sack, as do the large numbers of teachers who have joined a union-led boycott of the tests.

So far the reforms seem highly popular except, unsurprisingly, among the teachers. Edmund Gordillo, a teacher in Quito with 30 years' experience, complains that coercion is the wrong way to go about reforming. Others grumble at their meagre pay: a typical teacher, with almost 25 years' experience, earns only around $650 a month. The government is promising pay rises but, to the union's disgust, it intends to link them to performance, not seniority.

Ecuador's universities are also having to shape up. Low-quality private ones will be shut, while state-funded ones will have to account publicly for the $490m a year they receive. Professorships will be opened up to foreign academics. Mr Correa's reforms are non-negotiable, insists René Ramírez, his planning secretary: if the unions and student groups ramp up their protests, the government is ready to call a referendum to demonstrate that Ecuadoreans support the president's policies.

The Turks and Caicos loses independence

A very British coup

Aug 20th 2009 | PORT OF SPAIN
From The Economist print edition

Self-government is suspended amid reports of serious corruption

THE self-rule that the Turks and Caicos islands have enjoyed for 33 years was taken away on August 14th, when Britain removed their elected premier, cabinet and assembly, and suspended most of their constitution. For the next two years or so the islands, whose population is around 38,000, will be run by their governor—the representative of Queen Elizabeth.

Britain felt it had few choices, following the publication last month of a report by an inquiry, headed by Sir Robin Auld, a former British judge, which found a "high probability of systemic corruption" in the tiny country's government, with ministers apparently bribed by foreign property developers. Sir Robin described the situation as a "national emergency". He recommended a police investigation of Michael Misick, who resigned as premier in March but denies wrongdoing, and other government figures. The report noted Mr Misick's reputation for enjoying a "Hollywood lifestyle" and said his spending habits "far exceeded his salary and allowances".

Thirty years ago the islanders scratched a living from infertile soil, salt pans and fishing. White sands and clear waters have since spurred a tourist boom, with an added fillip from offshore finance. A steady flow of rich white expats and impoverished Haitians has swollen the population.

Dizzy economic growth has not, alas, brought political maturity. Voting rights are limited to adult "belongers"—broadly, the locally born—of whom fewer than 7,000 are registered. The assembly's 15 seats have electorates as small as 190. Politicians have built tight support networks with favours given and received. Mr Misick's now ex-wife, LisaRaye McCoy-Misick, told the inquiry he had handed out $100 bills to voters before winning a landslide majority in the February 2007 election. Privileged belongers have been sold crown land for as little as 25% of its market value, sometimes flipping it onwards to commercial developers. For those who lost favour, though, life could be difficult. A British parliamentary committee visited the islands in 2008 and found a "palpable climate of fear".

Mr Misick has called on islanders to "resist" British rule. Galmo Williams, who briefly succeeded him as premier, said the islands had been "invaded and recolonised" with a "dictatorship" like "the old Red China". The suspended opposition leader, Floyd Seymour, has "mixed feelings". But some locals are angry that Britain did not step in sooner. In July the Caribbean Community said meekly that a new election would be better than direct rule. The islands have been through all this before. The constitution was suspended in 1986 after an inquiry into arson and alleged corruption. Sir Robin's report noted how little had changed since then.

There has long been a debate on whether the Turks and Caicos and other micro-states in the region are viable as self-governing entities. For most of the imperial period the islands were run from Jamaica or the Bahamas. As Britain's Caribbean colonies were heading towards independence in the 1950s, there was a short-lived attempt to unite them all in a West Indies Federation, to be run from Trinidad (which has recently talked to some neighbours about a possible union). There have also been various suggestions down the years to unite the Turks and Caicos with distant Canada. Returning them to the mercies of chaotic Jamaica would offer few benefits. But the Bahamas, having made great strides in overcoming its own corruption and drugs problems of the 1980s, would seem a good candidate to take the islands back under its wing one day.

Japan's election

Railing against the wrong enemy

Aug 20th 2009 | TOKYO
From The Economist print edition

As an historic campaign starts, both main candidates take aim at free-market capitalism as well as each other

AP

SASHED candidates standing on car roofs, their voices crackling through loudspeakers. Worrying signs of heatstroke affecting one of the ruling-party's septuagenarians. Women applauding politely, wearing hats and long gloves to shield their pale skin from the glinting sun.

It was August 18th, the official start of campaigning for Japan's general election on August 30th. But it might just as easily have been 1960, when Yukio Mishima, one of Japan's greatest novelists, published "Utage No Ato" ("After The Banquet"), an evocation of a fictional August election with loudhailers, perspiring candidates and odd goings-on in "the bog of politics".

As the 12-day general-election campaign got under way (the first to be held in August in 107 years), there was something quaintly old-fashioned in the absence of television hoopla. In a country otherwise mad on mass-media, a musty-smelling ban on internet campaigning also recalled a bygone era.

Even the two main candidates for prime minister, Taro Aso of the ruling Liberal Democratic Party (LDP) and Yukio Hatoyama (pictured above), of the Democratic Party of Japan (DPJ), have hardly torn into each other. In debates, they have sounded more like two bickering old men than the scions of political dynasties (their grandfathers fought over the founding of the LDP in 1955) waging what could be one of the most important battles in any election in Japan's history.

Mr Hatoyama has tried to cast himself in the Barack Obama mould, using the English word "change" to sum up the DPJ's meaning to voters. After half a century of almost wall-to-wall rule by his rival's party, that should be an intoxicating message. The DPJ says evicting the ruling party will break the stranglehold on the budget held by mandarins, giving it freedom to cope with Japan's ageing population, the low birth-rate and a dangerously lopsided, export-oriented economy. But Mr Hatoyama's face hardly moves as he delivers the good tidings in a soporific murmur.

Mr Aso, meanwhile, has questioned the DPJ's ability to pay for expensive campaign promises, such as a ¥26,000 ($280) a month child allowance to push up the birth rate, income support to farmers and heavily subsidised schooling. The opposition party's sums are indeed fuzzy.

But opinion polls give the DPJ a two-to-one margin over the LDP. Even old ruling-party stalwarts such as doctors and construction workers are shifting allegiances, according to a survey by Kyodo, a news agency. Behind the scenes, analysts say DPJ strategists are working tirelessly to field fresh-faced, likeable candidates to stand against LDP dinosaurs. That has meant a high number of candidates are campaigning: 330 from the DPJ and 326 from the LDP. When parliament was dissolved last month, the LDP held 300 of the 480 seats and the DPJ just 115 (there is a host of smaller parties). In the most hopeful forecasts for the DPJ, some analysts think those numbers could be reversed.

The low-key nature of the race contrasts with the previous contest in 2005, which was swept by the LDP under Junichiro Koizumi, a former prime minister. In what was known as "Koizumi theatre", the telegenic reformer obtained extensive television coverage by replacing LDP candidates who opposed his plans to privatise the postal system. The DPJ hardly got a look in.

Mr Koizumi is playing a big role in this election too. He is not on the ballot, after shamelessly betraying his own anti-dynastic principles by bequeathing the right to run for his seat to his son. But he still looms large—these days, as a target for both Mr Hatoyama and Mr Aso. Both men appear more intent on laying into his legacy of free-market reforms, though some predated his rule from 2001-06, than on attacking each other. They blame his removal of a ban on temporary workers in manufacturing for soaring inequality and high rates of poverty in a country that used to pride itself on being almost universally middle-class. But neither has come up with a very convincing alternative.

In an article this month, Mr Hatoyama railed against American-led "market fundamentalism" that, he said, the LDP had embraced since Mr Koizumi's leadership. But his alternative is a mushy-sounding concept, *yuai*, that mixes up the Chinese characters for friendship and love. He calls it fraternity, and says it means that activities such as agriculture—already under Fort Knox-like protection in Japan—will not be left "at the mercy of the tides of globalism". Mr Aso has likewise pledged to break with "excessive market fundamentalism".

Such views have helped shape both parties' manifestos. The DPJ's policy platform, for instance, proposes undoing one of the main Koizumi reforms by banning the use of temporary labour in manufacturing. It also wants to raise minimum-wage levels. Exporters fighting for business in China deplore both policies. Yet analysts say Mr Hatoyama, who at a recent press conference asked an aide to field questions on economics, will have little influence on—or even interest in—economic policy. Also, an upper-house election is due in 2010. This may limit the DPJ's ambitions; its priority is likely to be restructuring the civil service, where it can most easily score political points.

Not everyone thinks Mr Koizumi's reforms are widely unpopular. The image of temporary workers losing their jobs, and sometimes their home, as the economy slumped last winter was a poignant one. But the stodgy LDP old guard, which had presided over two decades of economic stagnation, bore as much of the blame as the reformist Mr Koizumi.

Jiro Yamaguchi, of Hokkaido University in northern Japan, argues that Mr Koizumi, while trying to trim the budget deficit, failed to do enough to strengthen the social-security system to shield people from the effects of deregulated wages and job losses. He thinks the DPJ, which he advises, should concentrate on developing such "Third Way" reforms. But the party has not yet taken up this cause.

In one way, the DPJ has reason to be grateful to Mr Koizumi. By selling off the postal system, cutting pork-barrel spending to the construction industry and shrinking an already small state further, he may have at long last cut the financial lifeline linking the LDP to its core supporters. If so, then at least the DPJ will not have to endure a full replay of "Utage No Ato". In Mishima's novel, the party in front as the election campaign starts does not find it ends altogether happily.

Taiwan's typhoon

The political storm

Aug 20th 2009
From The Economist print edition

After its dismal handling of the disaster, the government, too, is covered in mud

Reuters

Still searching for where the bodies are buried

A FORTNIGHT after Typhoon Morakot first struck Taiwan on August 6th the storm continued to wreak havoc on the island. Extensive flooding and landslides had claimed some 500 lives, according to Ma Ying-jeou, the president, and caused at least $2 billion-worth of damage to property. About 400 people were thought to have died in southern Kaohsiung county alone. There, the authorities have given up hope of finding more survivors in Hsiao Lin, the hardest-hit village, which a landslide had buried in mud.

Morakot is also doing political damage. President Ma faces harsh criticism for his government's slow response to the disaster, and in particular for its surprising decision to spurn foreign offers of aid in the early stages. Three senior officials have already offered their resignations. The reputation of Mr Ma himself has taken a knock.

The first to offer up his political head was Andrew Hsia, a deputy foreign minister, who took responsibility on August 17th for the rejection of foreign offers of assistance. Two days later Chen Chao-min, the defence secretary, and Hsueh Hsiang-chuan, secretary-general of the cabinet, also offered to resign. A wholesale cabinet shuffle is to follow next month, and other senior officials may not survive in their posts even that long.

Mr Ma has long been seen as a smooth operator, able to glide unscathed through political turmoil. But this time the apologies he has made may not be enough to see him through. An opinion poll this week by TVBS, a Taiwanese news channel, showed a dramatic drop in his approval rating: by 25 percentage points since June, to an all-time low of 16%. Other polls give him higher ratings but show a similar decline.

Reinforcing this message, angry residents of Hsiao Lin angrily scolded Mr Ma on August 19th when he made his first visit there since the typhoon. Viewers across Taiwan saw the president quietly endure tongue-lashings from survivors and the bereaved. After a comfortable election victory, Mr Ma took office 15 months ago with promises to focus on the economy and improve ties with China. He has already given warning that Taiwan's third-quarter economic figures will suffer because of Morakot. But he has also promised a more efficient recovery effort and an investigation into the shortcomings in the government response. At least neither he nor his parliamentarians face elections this year, though there will be local polls.

In one striking proposal, Mr Ma said Taiwan's army would reorder its priorities towards handling big disasters. Now, he told a news conference, our enemy is not necessarily the people across the Taiwan

Strait but nature. Taiwan would cancel orders for American military helicopters and buy disaster-relief helicopters instead.

The ever-complex and ever-delicate relationship between Taiwan and China was bound to play a role in Morakot's political aftermath. For its part, China was quick to respond, not only expressing sympathy for the people it refers to as "compatriots" but also providing $29m in relief funds, prefabricated houses, sleeping bags and sanitation supplies.

Yet many people in Taiwan also saw China as the reason why the government had to think twice before accepting help from America or Japan. Hints that Taiwan might be enhancing its military or official links with other powers tend to provoke Chinese bluster. More likely, the government simply underestimated the scale of the disaster—the worst storm in 50 years. After all, on August 16th, an American cargo plane arrived. It was the first American military aircraft to land in Taiwan in the 30 years since America severed its diplomatic ties with Taiwan in favour of China.

Kim Dae-jung and North Korea

A glint of sunshine

Aug 20th 2009 | SEOUL
From The Economist print edition

Kim Dae-jung is dead but his policy of engaging North Korea is resurrected

AP

Still some sunshine when he's gone

THE mood among mourners is appropriately sombre. But there is an air of triumph among some of Kim Dae-jung's former confidants. The portrait of the late South Korean president, who died on August 18th, aged 85, sits on an altar, surrounded by white chrysanthemums. In it, he wears the hint of a smile. As he might: his widely criticised policy of promoting political and economic exchanges with North Korea may be about to be revived, albeit in limited fashion, by one of its fiercest critics, the current president, Lee Myung-bak. Partly as a consequence, a new sense of tentative optimism is lightening the gloom on the Korean peninsula.

The South's Mr Kim was the foremost proponent of engagement with North Korea as a means to bring lasting peace to the peninsula—what became known as his "sunshine" policy. Mr Lee, however, has been among the many South Koreans deeply sceptical about its perceived benefits. His government has voted in favour of a United Nations resolution condemning North Korea's human-rights record and lent strong support to international efforts to impose comprehensive economic sanctions against the regime in Pyongyang. Mr Lee insists there will be no big dollops of aid until North Korea starts disarming, as it promised under a 2005 deal. Yet he has welcomed news that a delegation from North Korea will attend Mr Kim's funeral.

That delegation appears to be part of a new approach by North Korea's dictator, Kim Jong Il. After provoking the world's wrath and economic sanctions by conducting a nuclear test in May, he is suddenly exuding friendliness. On August 16th he had a four-hour lunch in Pyongyang with a South Korean businesswoman, whom he had met three times previously, Hyun Jeong-eun, of the Hyundai conglomerate. Ms Hyun says he told her delegation to tell him everything they wanted, "So we did."

Ms Hyun claims to have wrung significant "concessions" from Mr Kim, though, as usual, most will benefit the North more than the South. North Korea will allow some separated families to hold a reunion. It will also allow South Korean tourists back into North Korea. And Mr Kim promised to allow commercial traffic across the border to resume, and to "energise" an industrial park run as a joint venture with South Korea at Kaesong in the North. South Korea is now pressing for official talks.

Kim Jong Il's change of tack followed his release earlier this month of two detained American journalists, during a visit to Pyongyang by Bill Clinton. The mission was supposedly "private". But Mr Clinton's status as a former American president and his wife's job as secretary of state in the present American administration suggested a diplomatic channel had been opened. Lee Su-hoon, the director of the Institute for Far Eastern Studies at Seoul's Kyungnam University, says Mr Clinton's visit prompted South Korea to re-examine its inflexible stance towards the North. President Lee had sought to exert pressure by shunning most political, business and other contacts.

This would have pleased Kim Dae-jung no end. He was widely praised for his bold initiative to meet his North Korean namesake in June 2000. The historic breakthrough won him the Nobel Peace Prize that year, although the achievement was sullied by the revelation that his government had in effect bought the summit by making large payments to North Korea. The company at the centre of arranging those payments was Hyundai.

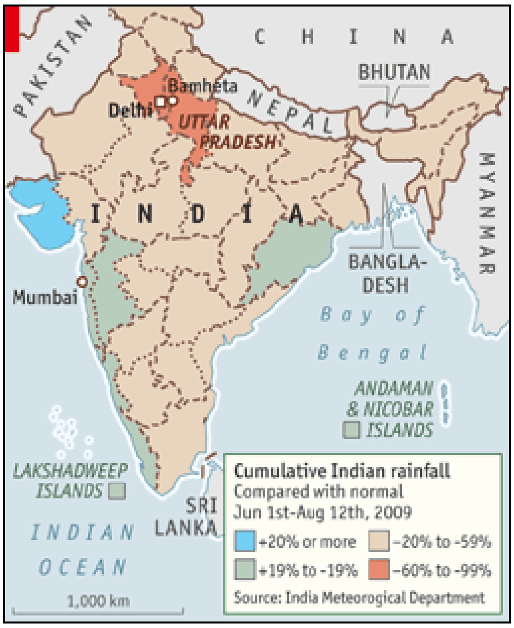
At his last public engagement in June, Kim Dae-jung defiantly defended his legacy. "There should be continued negotiations and patience" with North Korea, he said from a wheelchair. "Aid and compensation is needed for North Korea to give up its nuclear weapons." Despite Mr Kim's death, the debate continues about which—aid or renunciation—should come first.

India's failing monsoon

It never rains

Aug 20th 2009 | BAMHETA, UTTAR PRADESH
From The Economist print edition

An ancient curse strikes India



SHARMILA SHARMA, a farmer in the north Indian state of Uttar Pradesh, lounges with three sisters-in-law and six buffaloes in the broad shade of a neem tree. It is not the blistering heat that is keeping the women away from their land of a little over an acre (0.4 hectares). Like most Indian farmers, the Sharmas have no access to irrigation systems. They depend on the monsoon rains that fall between June and September. This year the rains have not come. "No rain, nothing," says Sharmila, as she flicks away flies with the edge of her scarlet sari. The family has been unable to plant its main sorghum crop, she says, and their buffaloes are becoming "diseased", a euphemism for starving.

India is experiencing its worst monsoon in years. Summer rains constitute around 80% of the country's annual rainfall. But from June to mid-August, when most crucial planting takes place, the rains were 29% lower than average. In Uttar Pradesh, they were down by more than 60%. Rice, the biggest crop sown during the monsoon, has been worst affected, along with sugar cane and oilseeds. Rainfall has increased in some areas in recent days. But it has come too late for many crops, which require an even sprinkling through the hot summer. Heavy showers now could even damage already reduced crops of sugar cane. Fresh rainfall may prove more helpful to winter-sown crops such as wheat, which rely heavily on water from reservoirs, whose levels remain far below average. To mitigate the damage from the poor monsoon, the government is encouraging farmers to plant more winter crops.

India's economy is closely tied to its fickle summer rains. Agriculture accounts for 18% of GDP. More importantly, it employs 60% of Indians, many of whom now seem certain to curb their spending this year. A bad monsoon can also reduce power production: hydropower provides a quarter of India's electricity. In 2002, when monsoon rains were down by 19%, GDP growth slowed from 5.8% to 3.8%. But as agriculture shrinks as a proportion of GDP—it made up 30% in 1990—the impact of poor monsoons is reduced. This year industrial output in June surged by its highest annual rate in 16 months, nearly 8%. Still, many economists have shaved a percentage point off growth estimates for the year, to between 6% and 7%. The government, meanwhile, has said it has enough food stockpiled from two years of healthy harvests to prevent high inflation.

For farmers, the effects of a poor monsoon are painfully clear. Most are smallholders, who fall easily into debt, and a dry summer can mean ruination. The government has said it will increase food subsidies to rural areas and allow farmers to delay paying bank loans. It may also pump more cash into a job scheme that guarantees 100 days work a year to every poor rural Indian family. Last year, it spent nearly 700 billion rupees ($14.3 billion) on waiving farms loans for impoverished farmers; there is no plan for a new scheme this year.

But two clear signs that farmers are in "extreme distress" are emerging, according to M.S. Swaminathan, a scientist revered as the father of India's green revolution. Cattle sales are rising steeply, even though prices are pitifully low. "And many more farmers are committing suicide."

Australia's relations with China

Different approaches

Aug 20th 2009 | SYDNEY
From The Economist print edition

Not quite a love-in, but too important for a dust-up

AP

Kadeer irks China, just by being there

WHEN Kevin Rudd, Australia's Mandarin-speaking prime minister, came to power in late 2007 the country's relations with China seemed poised to improve. But the love-in has failed to happen. This week Australia's government announced that China had cancelled a visit by He Yafei, a foreign-affairs minister, earlier this month. He was to attend a summit of Pacific island leaders, at which Mr Rudd hoped to discuss his plan for a new Asia-Pacific regional body involving China.

The snub was the latest setback in a relationship undergoing strains on several fronts. Australia's commercial relations with its biggest trading partner tend to collide with China's unhappiness over its political stance, especially over human rights. The cancelled ministerial visit was a response to a decision to allow Rebiya Kadeer, an exiled activist from China's ethnic Uighurs, to visit Australia.

China has accused Ms Kadeer of inciting riots involving Uighur and Han Chinese last month. Her visit was to attend the opening of an Australian film about her at the Melbourne Film Festival. The organisers ignored pressure from Chinese officials to cancel the screening, moving it instead to a larger venue when publicity over the row fuelled demand. China reportedly threatened Melbourne's mayor with ending a sister-city relationship with Tianjin. It also unsuccessfully leant on the National Press Club in Canberra to cancel an invitation to Ms Kadeer to speak there.

Yet this week another Australian minister was in Beijing for the signing of a deal under which China will buy liquefied natural gas worth A$50 billion ($41 billion) from Gorgon, off Western Australia's coast. The deal between PetroChina, a state-controlled company, and Exxon Mobil is reckoned to be Australia's biggest-ever trade contract. There are hopes that China might be signalling that commercial pragmatism will dictate relations with Australia.

It is proving hard, however, to disentangle the commercial from the political. In June China was upset by what it saw as a threat to its interests when Rio Tinto, an Anglo-Australian mining giant, walked away from an offer by Chinalco, a state-run aluminium firm, to pay $19.5 billion to double its stake in the firm. Instead, Rio struck a deal with BHP Billiton, its main competitor, to exploit jointly the vast iron-ore deposits of Western Australia's Pilbara region. Already, China is Australia's biggest market for iron ore, to fuel its industrial expansion.

Australians mainly welcomed the collapse of the Chinalco deal, amid perceptions that China wanted to use its economic power to exert pressure on prices of one of the country's most lucrative resources. Scepticism towards China in Australia hardened in July after the detention of Stern Hu, an Australian who heads Rio's iron-ore operations in China, and three colleagues. Initially accused of stealing state secrets, seemingly to help Rio's bargaining position in the annual benchmark pricing negotiations for iron ore, Mr Hu and some colleagues were eventually charged this month with the lesser offences of commercial espionage and taking bribes.

Reflecting his own background as a diplomat in China, Mr Rudd has taken a low-key approach to resolving the affair of Mr Hu. An opinion poll published this week found that 58% of Australians approved of Mr Rudd's handling of China. But China's recent tough tactics may have done little to reassure Australians about the intentions of their giant trading partner. *China Daily*, a state-run newspaper, this week accused Australia of being "the champion leader of anti-China chorus". That chorus is unlikely to pipe down.

Economist.com WORLD ASIA

A murder in China

Crime and punishment

Aug 20th 2009 | LISHI
From The Economist print edition

An everyday tale of abusive Chinese officialdom and violent revenge

A VALLEY settlement in the uplands of north-central China's Shanxi province, Lishi presents a prosperous face that China's modernising leaders might be proud of. Shining cars throng the main street, where a recently completed shopping arcade is fast filling with tenants. Proliferating building sites testify to the march inland of China's long coastal boom.

Yet a murder trial due to start on August 25th suggests that behind the façade of modernity lies a political culture rooted in the imperial past. As locals tell it, for ten years until last autumn, citizens just one kilometre up the valley in the village of Xiashuixi lived in fear of Li Shiming, a corrupt and rapacious local Communist Party secretary. One of his victims was Zhang Waixin, a local farmer. One day in 2004 he found Mr Li and two of his five brothers digging up the crops on his land, and tried to stop them. The three men beat him so badly he was hospitalised. On discharge, he found his land had been cleared and marked out for a housing development.

Another local, Li Weibin, says that after this, when mixing cement on another coveted plot, he was attacked by thugs employed by the party boss. He spent four months in hospital with injuries including a broken hip bone. He says he was one of many who got in Li Shiming's way, and one of many in the area who hated him.

Wang Hou'e and her family suffered especially badly. She was arrested when she tried to lead a group of 24 farmers to Taiyuan, the provincial capital, to protest against the village leader's confiscation of their land. She was thrown into prison, where she was beaten every three days and later contracted tuberculosis. On the day of her release in 2003, she discovered Mr Li had used his influence to have her 13-year-old son, Zhang Xuping, expelled from school. He drifted into petty crime and was later sentenced to one year in prison for acting as lookout to a gang of thieves. In jail he was tortured and tried to kill himself. Thereafter Mrs Wang's family was subjected to continuing harassment because she persisted in appealing to the provincial and national authorities for justice.

Sadly, none of this is unusual in China. The illegal seizure by local party officials of valuable farmland at the edge of burgeoning cities is a rampant and growing abuse. On September 23rd last year, however, this saga took an unusual turn. Mrs Wang's son, Zhang Xuping, the expelled schoolboy, met another victim of Mr Li's land grabs. The encounter took place outside a school where the village chief was attending a meeting. The aggrieved farmer gave the younger man 1,000 yuan ($147) in cash and a knife. The teenager entered the school, found his family's tormentor alone and stabbed him through the heart.

Zhang Xuping confessed to his crime and now faces trial at the intermediate people's court in Luliang. His offence is serious. In China, many criminals are executed for far less. But a further feudal twist to the tale may save his life.

Histories of China relate many instances of imperial pardons for upright individuals who get rid of an evil official, after a mass of citizens testify to the slain mandarin's wickedness. So, after seeing one such episode featured in a popular historical soap opera on television, Zhang Xuping's brother started his own "10,000- name defence". To date he has collected just under 21,000 signatures.

Even in Communist China, the approach may work. There is no precedent for a presidential pardon. Nor are there provisions in criminal law for petitions. Yet they are so common that this week the government issued a regulation to stop petitioners coming to Beijing. It is mindful of the huge scale of local corruption,

of the lack of recourse open to its victims and of the simmering hatred it engenders. That helps explain an appeal to China's judges by the chief justice in April 2008 to consider the "feelings of the people" when handing out sentences. In June this year, a court in the central province of Hubei complied, by acquitting a 21-year-old pedicurist who had stabbed a sexually abusive official to death. Her case had generated a huge internet-fuelled outcry and publicity, including protests in Beijing.

"There's no doubt that if a petition is big enough it will influence a court," says Yu Ping, a researcher on Chinese criminal law at New York University. Mrs Wang and her family are poor, with limited knowledge of the law. Yet their instinctive understanding of how to sway the Chinese judiciary may serve Mrs Wang's son well.

China's drink-driving crackdown

Call a cab

Aug 20th 2009 | BEIJING
From The Economist print edition

Or stick to tea. It's a jungle out there on China's roads

Illustration by Claudio Munoz

AMONG the first motor cars ever imported to China was a new handmade, wood-bodied 1901 Duryea, brought from America as a gift for Cixi, the empress dowager, to mark her 66th birthday. Setting a rather inauspicious precedent, the empress is said to have fortified her driver, Sun Fuling, with a generous bowl of rice wine. Mr Sun promptly lost control of the newfangled thing, running over and killing an unfortunate palace eunuch.

In the service of the empress, this inept chauffeur faced no legal sanction for the mishap. Modern-day offenders, whose numbers, sadly, are increasing, are not so lucky. Sharing the surname but not the legal immunity of China's first recorded drink-driver, Sun Weiming, a 30-year-old executive, was heavily under the influence last December when he killed four people in a crash in the province of Sichuan. On July 24th he was sentenced to death, though he is now hoping a deal to compensate the families will be enough to save his life.

Public opinion in China is divided over whether the sentence is appropriate. But the harsh handling of his case may not be a one-off. Chinese police have launched a nationwide crackdown, promising stricter laws, tougher enforcement and sterner punishment—no matter who the offender may be. "Let drink driving be a high-tension line that no one dares to touch," declared Liu Jinguo, a deputy minister of public security.

On the weekend of August 15th-16th, police in cities across China stepped up random traffic checks and breath tests. They caught 3,167 drivers who had been drinking, including 435 with a blood-alcohol concentration above 0.08%, China's legal limit. At that level, drivers may be jailed for 15 days, stripped of their licence for six months and fined 2,000 yuan ($294).

A two-month campaign has been launched, linked to grand celebrations planned to mark the 60th anniversary on October 1st of the founding of the People's Republic of China. During this period, drivers with any blood-alcohol concentration above 0.02% will also be penalised. Officials say alcohol played a role in a quarter of China's 265,000 traffic accidents this year, and that drink-driving cases rose 9% in the first half of the year over the same period in 2008.

Because of the steady rise in the number of people with driving licences, that increase may not imply a higher proportion of drink-drivers. But given the ever more congested state of China's roads, negotiated by so many inexperienced new drivers, the authorities' intervention seems overdue. In order to make the nation's 60th birthday less deadly than Cixi's 66th, drivers would do well to make their toasts in fruit juice.

Economist.com
WORLD
MIDDLE EAST & AFRICA

Libya and Muammar Qaddafi, 40 years on

How to squander a nation's potential

Aug 20th 2009 | CAIRO
From The Economist print edition

Their Great Leader is less of a pariah now, but that hasn't helped Libyans much

AP

AUTUMN should be looming for Libya's ageing patriarch. Since seizing power 40 years ago, Muammar Qaddafi has survived wars with neighbouring countries, repeated assassination plots and years of siege under international sanctions, along with much of the world's opprobrium and even ridicule. Yet, as he prepares to celebrate the anniversary on September 1st of the coup against King Idriss that he led as a young army captain back in 1969, this looks more like springtime for Libya's strongman. Flamboyant as ever despite his wrinkled face and rambling speech, he is increasingly fawned upon.

Since the passing of President Omar Bongo of Gabon in June, Mr Qaddafi has no near rival as the longest-serving African or Arab leader, and longevity seems to feed his ambition. Last year, having staged a jamboree of traditional rulers at his hometown of Sirte on the Libyan coast, where he is said to have been born in a Bedouin tent, he had himself proclaimed king of Africa's kings. He currently presides over the African Union, which he is pushing to live up to its name and turn somehow into a continent-wide United States of Africa, presumably with himself in charge.

Such assertions of grandeur still produce sniggers, but Mr Qaddafi can claim to have chalked up numerous recent diplomatic successes. Libya currently sits as a rotating member of the United Nations Security Council, a privilege inconceivable in the years when President Ronald Reagan described Mr Qaddafi as a "mad dog". The Libyan leader's first-ever trip to America, expected later in September for an address to the UN General Assembly, will mark a further sign of return from pariahdom. This follows Mr Qaddafi's recent appearance on the margins of a G8 summit, and visits to him by the leaders of Britain, France and Russia, as well as America's then secretary of state, Condoleezza Rice.

Such prizes are rewards for a decade-long effort to extract Libya from the limbo into which Mr Qaddafi had led it through his dabbling in terrorism and his reckless support for radical causes, including those of various unsavoury Palestinian factions and the IRA. The comeback started with the Libyan leader's acceptance of blame for the 1988 bombing of an airliner over Lockerbie as well as for the similarly grisly 1989 bombing of a French aircraft. But Mr Qaddafi's big break came after the terrorist attacks on America in 2001. Having faced down its own jihadist insurgency and been the first government to request an international arrest warrant for Osama bin Laden, the Libyan regime joined enthusiastically in the Bush administration's "war on terror". As America plotted to invade Iraq, asserting that the country's alleged weapons of mass destruction represented an immediate danger, Libya, caught out in its own nuclear

dabblings, set what was seen as a salutary example by declaring it would not only abandon its secret weapons programme, but also expose its network of suppliers.

Mr Qaddafi is reaping rewards for his reformed behaviour at home too. Tripoli, Libya’s capital, is sprouting fancy new hotels, as well as a new airport, to welcome an influx of would-be investors and tourists. Literacy is now nearly universal among schoolchildren. Life expectancy has gone up by 20 years, and infant mortality has fallen to less than a tenth of the level it was at the time of the revolution.

Yet such gains ought to be unremarkable for a country that exports nearly as much oil, per head, as Saudi Arabia: a total of $46 billion-worth last year, divided among just 6m people. In fact, Libya trails far behind other oil-rich states by many measures, and not just in the contrast between Tripoli’s garbage-strewn thoroughfares and the gleaming Miami-scapes of the Gulf. As any Libyan who recalls the days before Mr Qaddafi’s revolution can attest, this is a country where something has gone very wrong.

Things are not so bad as in the dark days of the 1980s, when the Great Leader experimented with ruinous social theories and had dissidents hunted and shot. Yet while Libya’s peculiar form of socialism still brings free education and health care, along with subsidised housing and transport, trade unions remain banned, along with nearly every kind of independent social organisation. Salaries are extremely low, thus keeping Libyans cash-poor even as billions stack up in foreign reserves, or in the pockets of a narrow band of regime insiders. A lack of jobs outside the government has led to youth unemployment of perhaps 30% or more (all statistics in Libya are as blurry as a Saharan sandstorm).

Such shortcomings reflect more than simple inefficiencies. Mr Qaddafi’s Libya is a country that has been systemically mismanaged for a generation, at virtually every level of government. And among other systems that have no clear order is the one for deciding who will succeed him. Two of Mr Qaddafi’s seven sons are generally considered candidates, though the star of Saif, the elder son who has taken an interest in human-rights issues, appears to be waning in favour of Mutassim, whose lower profile disguises a powerful role in the security services. Both are thought to have strongly influenced their father’s mellowing trend in recent years. But it will take more than pots of cash and calmer ties with the West to bring Libya anywhere close to meeting its potential.

Israeli politics

Bibi the happy juggler

Aug 20th 2009 | JERUSALEM
From The Economist print edition

Binyamin Netanyahu soaks up the pressures from abroad and at home

IT HAS been a good summer for the Israeli prime minister, Binyamin Netanyahu. Five months into his term, his centre-right coalition looks solid, and he himself exudes an air of confidence. But more anxious times lie ahead as the Obama administration prepares to publish its own plan for peace between Israel and the Palestinians. A first draft will be unveiled in September, according to Egyptian officials who travelled with President Hosni Mubarak to Washington this week. Mr Netanyahu's team expect the moment of truth in October. They are not looking forward to it.

For now though, Mr Netanyahu's optimism stems from the fact that he is getting the domestic politics right. None of his coalition partners is threatening to walk out on him, an unusual bonus in Israeli coalitions where the partners-cum-rivals are forever eyeing alternative alliances. The fractured arithmetic of the present Knesset has led the politicians to conclude that Mr Netanyahu is the only realistic option, other than elections which no one wants to trigger so early in the term.

Mr Netanyahu has reinforced this reality by ramming through the Knesset a law that would enable seven members of a large party to secede as a block, and to take their state financing with them. It just so happens that Mr Netanyahu believes that seven members of Tsipi Livni's Kadima, the main opposition party, may secede and join his coalition. Mr Netanyahu brushes aside accusations of unfair play. He says Ms Livni would do the same to his Likud if their roles were reversed.

In terms of policy, Mr Netanyahu has managed to juggle pressures from America and political pressures at home into a convenient holding pattern. An early confrontation with President Barack Obama over settlements has softened over the summer into an ongoing negotiation with the president's Middle East envoy, George Mitchell, over how long and how extensive an Israeli building freeze might be. Building, by private contractors, goes on meanwhile in many of the settlements. Yet Mr Netanyahu won praise from Mr Obama on August 18th for an unannounced suspension of government-sponsored building projects. This was "movement in the right direction," the president said, as was Israel's removal of some of the checkpoints that hamper free movement for Palestinians on the West Bank.

Mr Obama also pointed to "increased economic activity" on the West Bank and praised the efforts of the American-trained Palestinian security forces which, he said, had "inspired confidence not just among the Israeli people but among the Palestinian people." A steep decline in terror attacks against Israelis has boosted Mr Netanyahu's standing at home and contributed to a widespread feeling that the conflict with the Palestinians is being contained and the dispute with Washington successfully smoothed over.

However, an Obama peace plan could sharply disturb Mr Netanyahu's mood of calm. Just how sharply was signalled this week by four of his more hawkish ministers who chose to tour several of the "illegal" settlement-outposts on the West Bank which the government has pledged to dismantle. These settlements were not illegal, the leader of the ultra-Orthodox Shas Party declared. Moshe Ya'alon of the Likud, one of Mr Netanyahu's two vice-prime ministers, said the government should seriously consider restoring the settlement of Homesh which Israel dismantled as part of Ariel Sharon's unilateral disengagement from Gaza and the northern West Bank in 2005.

Mr Netanyahu's office said nothing. Officials there would like the summer never to end.

More bombings in Iraq

Lethal and relentless

Aug 20th 2009 | BAGHDAD
From The Economist print edition

Militants strike at the heart of the capital

AP

The former foreign ministry

AT 10am on August 19th simultaneous car bombs and rocket attacks targeted half-a-dozen government offices. The foreign ministry was destroyed by an explosives-filled lorry that also set ablaze the surrounding buildings. A bomb smuggled into the education ministry narrowly missed killing the minister in his office, and a mortar landed near the home of the environment minister. Rockets fell across the heavily fortified Green Zone, destroying parts of the parliament building and damaging a neighbouring luxury hotel minutes before the prime minister was due to visit. At least 95 people were killed and over 500 more injured, among them many officials from the foreign ministry.

This was the worst act of violence in Iraq since American troops started withdrawing in June. For a few hours it took the capital back to the chaos and fear that reigned three or more years ago. Clouds of black smoke hung over the airless city. The Iraqi government says Sunni extremist groups including al-Qaeda are responsible, and they are indeed the most likely suspects.

This week's attacks were a direct challenge to the authority of the Shia-led government. National elections will take place in less than six months, and failure to show improvements in security will hurt the government's chances of winning another term. Nuri al-Maliki, the prime minister, has staked his political future on making Iraqis safe; with every bomb, the militants come closer to toppling him at the polls. Hence many Iraqis now expect violence to worsen in the run-up to the election scheduled for January 30th. Attacks have been on the rise, mostly focused on rural areas and the urban poor. Now the militants have switched from attacking the most vulnerable Iraqis to attacking the most heavily defended, thus increasing the pressure still further on the Shia politicians.

The rising violence seems to mock the prime minister's policies. Earlier this month he announced the removal of protective concrete blast walls in Baghdad; this helped the foreign ministry bombers. The escalation of violence is so serious that the American army this week announced plans to send its troops back into rural parts of northern Iraq where Kurds and Sunni Arabs are close to fighting over oil-rich land. All this comes only six weeks after America handed control of major towns back to the Iraqis. President Barack Obama has again pledged to have all American combat troops out of Iraq within 12 months. That seems rash now.

Economist.com
WORLD
MIDDLE EAST & AFRICA

An Ethiopian singer freed

Movement of jah people

Aug 20th 2009 | NAIROBI
From The Economist print edition

The country's Bob Marley can return to what he does best, at a price

Reggaephotos

IT WAS a euphoric week for younger Ethiopians. The country's great long-distance runner, Kenenisa Bekele, ran down an Eritrean rival to win gold in the world athletics championships. Even better, the country's most popular singer, Teddy Afro, was released from prison.

Ethiopia's prime minister, Meles Zenawi, says there are no political prisoners in his country. Human-rights activists and diplomats say there are thousands—and a lot of Ethiopians believe Mr Afro was one of them.

Mr Afro was jailed for a hit-and-run incident in 2006, despite always insisting that he was not in the car which the prosecution said knocked down and killed a homeless man in Addis Ababa. He served 16 months of a two-year sentence, which had already been reduced on appeal from six years on grounds of shaky evidence. His supporters, though, allege that his jailing had more to do with his third album, "Yasteseryal", released just before the country's last election in 2005. A lusty patriot who often sings, with funk and reggae influences, in praise of Ethiopia's deposed emperor, Haile Selassie, Mr Afro got into trouble for songs which compared Mr Meles's lot to a brutal junta.

The decision to release him was probably pragmatic. The government knows that it will have to win over unhappy young voters—Mr Afro's fans—if it is to win next year's general election convincingly. Officially, the singer's release was for good behaviour. But it was probably also conditional on his avoiding political songs in the run up to the election. Mr Afro seems to be playing along, at least so far. He told the state media that he had a "nice" time in prison.

The worry for the government is that the release of Mr Afro will now throw the spotlight back on its jailing of Birtukan Mideksa, a charismatic young opposition leader, judge and single mother. Ms Mideksa had already spent 18 months behind bars before she was jailed again earlier this year for denying that she had asked for a pardon. Her supporters say she has had to spend much of the year in solitary confinement.

Zambia's corruption trial

Not guilty

Aug 20th 2009 | LUSAKA
From The Economist print edition

A former president is cleared of corruption charges

AMONG the dog-eared exhibits on the upper floor of Lusaka's National Museum is a faded 1991 poster for Frederick Chiluba's Movement for Multiparty Democracy, asking "How long must we live off the crumbs of corruption?" At the time Mr Chiluba represented great hope for change in Africa, as his country became one of the first on the continent to embrace competitive multiparty politics. Although he was a diminutive former bus-driver, he ousted the independence leader, Kenneth Kaunda, in a landslide at the ballot box.

Mr Chiluba went on to liberalise the economy, but during and after his decade in office more commonplace tendencies in African governance began to emerge. He tried, and failed, to change the constitution to enable him to stand for a third term. Two years ago the High Court in London found, in a civil suit brought by the government of his hand-picked successor, Levy Mwanawasa, that he had stolen $46m from the state while in power.

This week, after a six-year process, criminal proceedings against him in Zambia itself for the theft of government money finally reached a verdict. It was the first time that an African former head of state had faced a credible trial in his own country for such offences. The case concerned a secret bank account that also featured in the London hearings, yet on August 17th Mr Chiluba was cleared of all six charges against him.

The prosecution argued that state money transferred to the account had been paid to beneficiaries who included Mr Chiluba's children. The defence, though, argued that more than $8.5m of private "gifts" to the president, some as large as $1m, had also gone through the same account, and that these were for Mr Chiluba to spend as he wanted. In the event, the court ruled that the prosecution had failed to prove that the $500,000 of disbursements at issue had come from government funds rather than out of Mr Chiluba's own money.

Mr Chiluba's spokesman, Emmanuel Mwamba, explained that "our law doesn't limit gifts to the president. In America, for example, the president can't receive more than $75. In our country, it is limitless how much Dr Kaunda received, how much Dr Chiluba received, or President Mwanawasa or [the incumbent] President Rupiah Banda," before pointing out that your correspondent could donate $100 if he so wished. "He will be very grateful."

Mr Chiluba denounced the trial as the work of "imperialists" in Britain. He says the charges were politically motivated. Anti-corruption campaigners were disappointed. "The case has proven that in Africa to fight corruption is very complicated," said the executive director of the Zambian chapter of Transparency International, an anti-graft watchdog.

Several factors make it so. Zambia's anti-corruption drive was started by Mr Mwanawasa but under Mr Banda the impetus from the top appears to be waning. As well as that, there is the traditional deference to leaders across Africa. A businessman in Lusaka lamented the way that government contracts are allocated, but added of Mr Chiluba: "It's an insult to involve him in such things [prosecutions]. He was head of state and we need to give respect to that position."

Former Yugoslavia patches itself together

Entering the Yugosphere

Aug 20th 2009 | BELGRADE
From The Economist print edition

Almost 20 years after political bonds were severed by war, day-to-day links between companies, professions and individuals are quietly being restored

AP

AT A recent summit of the cold-war relic called the Non-Aligned Movement, Serbia's president, Boris Tadic (above left), remarked that companies from former Yugoslav republics should join forces to bid on construction projects or specialised military-equipment contracts. His Croatian counterpart, Stipe Mesic (right), responded approvingly. Companies from "our countries", he said, were too small to compete in other markets by themselves.

On the face of it, these comments were both obvious and inconsequential. The firms are indeed small by global standards. Yet the use of the term "our countries" by the leader of one ex-Yugoslav republic to refer to everyone in the group, enemies as well as friends, points to a bigger change. From Slovenia to the Macedonian border with Greece, most people in the region still have a lot in common, even if they do not talk about it much. Every day the bonds between them, snapped in the 1990s, are being quietly restored. Yugoslavia is long gone; in its place a Yugosphere is emerging.

This huge shift in the daily life of the western Balkans is happening without fanfare. Few people have even noticed it. Those within the sphere take it for granted. Those outside are blithely ignorant. Perhaps that is not surprising. Good news is no news: the preparatory meeting to set up a south-east European firefighting centre, part of the Regional Co-operation Council, is hardly worth mentioning even in Sarajevo (where it took place), let alone anywhere else.

Yet it is precisely the fact that soldiers who were fighting one another not long ago now train together, or that firemen co-operate on a routine basis or that everyone from vets to central bankers meets with almost dreary regularity which constitutes the good news. That Regional Co-operation Council in Sarajevo has been patiently ploughing through a mass of dull, necessary work. It is a process, not an event.

The Yugosphere has its roots in shared experience, in trade and in business. Most former Yugoslavs—Bosnians, Serbs, Montenegrins and Croats—speak the same language with minor variations. Many Macedonians and Slovenes still speak or understand what used to be called Serbo-Croat as a second language. Within most of the region, people can travel freely using just their identity cards.

They like the same music and the same food. Political, religious and ethnic differences persist of course. But every summer thousands of young people come together at the Exit music festival in Novi Sad in

Serbia, and big stars from across the region have no trouble packing in audiences wherever they perform. Much to the irritation of Croatian music executives, the mobile phones of many young Croats hum with the latest Serbian tunes. Pan-Balkan opinion polls show a certain commonality of outlook: people have similar fears, worries and hopes. Gallup's Balkan Monitor, for example, released a survey in June that showed a drop in those wanting to emigrate in every state in the west Balkans.

Almost a third of Montenegro's trade is with Serbia. Bosnia is Serbia's largest export market and Croatia's second largest. Serbia is Macedonia's largest trading partner. In small economies, expansion generally means doing more business with the neighbours. Delta from Serbia, Mercator from Slovenia and Konzum from Croatia all run supermarkets and have been opening new shops in each other's backyards. Like more and more companies of the former Yugoslavia, they treat the region as one. Serbia's leading daily, *Politika*, has a domestic edition and a slightly different "ex-Yu" one. A typical recent Serbian headline announced the planned "conquest" of Croatia, not by armed force but by Cipiripi, a Serbian chocolate spread.

Some people always knew it would be thus. During the darkest days of the Yugoslav wars, criminals traded everything from guns to cigarettes across the front lines. What was known as "turbofolk" music was popular everywhere, even with its often nationalistic connotations. Now everyone else has caught up with the criminals and their turbofolk-singing molls. Serbs' biggest gripe about Croatia today has nothing to do with territory or refugees but the informal barriers which, they say, make it easier for Croatian companies to work in Serbia than vice versa.

Croats look stony-faced if you ask them about the Yugosphere. But not because they do not want it. They merely dislike the name, because it reminds them of the state they broke away from. No one else seems to mind, though. Even the former Yugoslavia's Albanians, who live mostly in Kosovo and Macedonia (and who are odd ones out in many ways), are not exempt from the Yugosphere's influence. An advertising executive from Albania says he could never market Italian milk successfully in Kosovo because, for Kosovars, Slovene milk is the gold standard.

In daily life, of course, many people live happily in more than one sphere. Kosovars watch television in Albanian but enter the Yugosphere when they trade with Serbia or go on holiday in Montenegro. Bosnians of all stripes eat the same things and do a lot of business together. But football brings out their differences, just as it does in many countries. Bosnian Serbs support Serbia's national football team, Bosnian Croats Croatia and only the Bosniaks (Bosnian Muslims) support Bosnia.

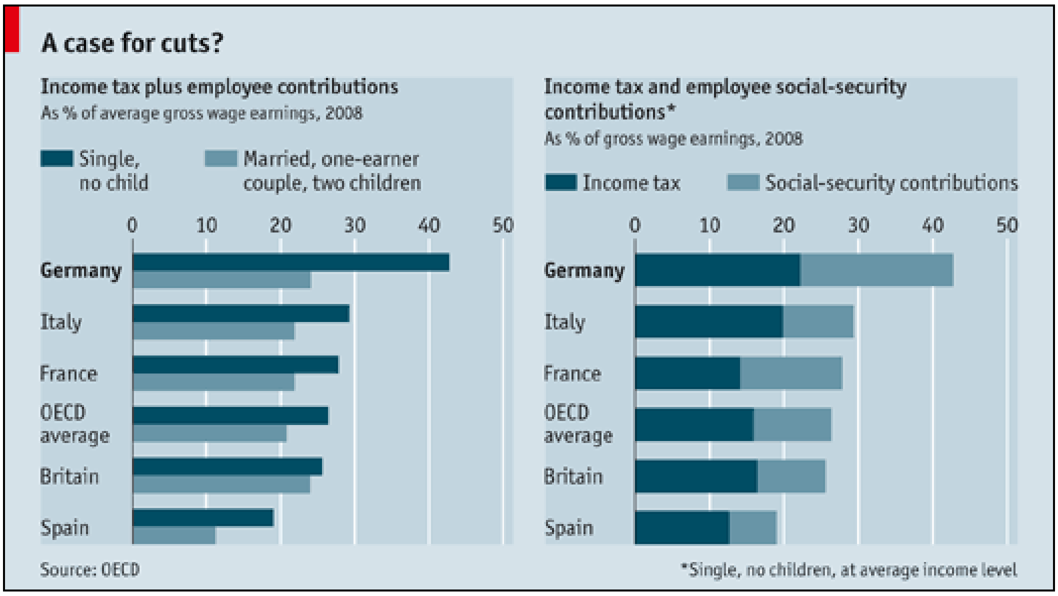
The trick over the next few years will be to consolidate what people have in common, keep their governments focused on that, and try to bring the region's politics and business more closely aligned both throughout the Yugosphere and, ideally, with the rest of Europe, too. The European Union was founded to cement peace on the continent and in the Yugosphere that job is not yet finished.

Germany's election

The parties' tax tangle

Aug 20th 2009
From The Economist print edition

Tax cuts emerge as a central issue in the election campaign



WITH little more than a month to go before Germany's parliamentary election, the Social Democratic Party (SPD) has so far failed to draw Chancellor Angela Merkel into a fight. Its chairman, Franz Müntefering, accused her of not caring about jobs, which sounded silly (the SPD says it will create 4m by 2020). Ms Merkel did not rise to the bait. Her plan is to shun the grubbiness of campaigning as long as she can and hope that on September 27th her personal popularity propels the Christian Democratic Union (CDU) back into power at the head of the next coalition government.

On one subject, though, the CDU seems willing to offer battle: taxes. Its election manifesto promises taxes that are "simple, low and fair". Ms Merkel flatly rules out tax increases to narrow the gaping deficits caused by the economic crisis. Her preferred coalition partner, the liberal Free Democratic Party (FDP), would go further, demanding a drastic overhaul of the income-tax system. Its leader, Guido Westerwelle, insists he will sign no coalition agreement that does not bind the next government to tax reform. The SPD, meanwhile, derides such plans. They have "no chance", says the Social Democratic finance minister, Peer Steinbrück. Currently the junior partner in Germany's "grand coalition" government, the SPD suggests a bit of relief for lower-income taxpayers but wants to raise the tax on the rich and to impose one on stockmarket trades.

Whichever coalition takes power after the election will face painful choices. The public sector balanced its books in 2008 but there is likely to be a deficit of 4.7% of GDP this year and 6% in 2010. Public debt will rise from 66% of GDP to 84%. Some countries are in even worse shape but by German standards these numbers are horrific. As a member of the euro zone, Germany's public-sector deficit should normally be no more than 3% of GDP. Gradually it will have to squeeze into an even tighter corset of its own making: under a new constitutional amendment, the federal government must cap its structural deficit (ie, adjusted for the economic cycle) at 0.35% of GDP by 2016; the 16 *Länder* (states) must eliminate theirs by 2020. At the same time, the main parties want to invest more in things like education and research. If the CDU and FDP are in charge, all this must somehow be reconciled with tax relief.

Taxpayers certainly deserve a break. A single person earning an average income pays more of his wages in income tax plus social-security contributions in Germany than almost anywhere else in the rich world. When they talk about taxes, Germans sound like they are discussing diseases. "Middle-class paunch" is the steep rise in tax rates at relatively low levels of income; "cold progression" means being pushed into

higher tax brackets by inflation. Taxpayers earning just 1.3 times the average income pay the "top rate" of 42% (in fact there is an even higher rate for very high incomes). The bureaucracy required to pay corporate tax costs companies €20 billion ($28 billion) a year, they complain.

The CDU and FDP vow to relieve these ailments but there is a big difference between them. The CDU, for all its talk, is offering little relief. It wants to cut the lowest tax rate from 14% to 12% and to introduce the top rate at a slightly higher level of income. The FDP would sweep away a thicket of tax rates, leaving just three: 10%, 25% and 35%. That would be expensive. The FDP puts the cost of its income- and corporate-tax proposals at €35 billion. "The FDP is offering a substantial change, while all the others are marginal," says Nils aus dem Moore of RWI-Essen, an economic-research institute.

The party insists the money can be found. It has proposed 400 spending cuts worth €10.5 billion and predicts that lower rates will lure part of the €350 billion black economy out of the shadows, allowing it to be taxed. Above all, the party says, lower taxes will provide incentives to work, which will boost economic growth, fill the state's coffers and narrow the deficit.

Social Democrats accuse the would-be tax cutters of pandering to the rich. Close to half of Germans pay virtually no income tax; for low earners the main misery is social-security contributions. Reducing these would give them relief while lowering the cost of employment. But the state may not be able to afford relief of any sort. Even if the economy bounces back from recession more quickly than expected, the government will struggle to meet its deficit-reduction targets. The federal government's finance plan calls for an annual reduction in the structural deficit of 0.2% of GDP starting in 2011. "There's no room to cut taxes during the next parliament," says Michael Bräuninger of the Hamburg Institute of International Economics.

Ms Merkel seems to realise this. The CDU's Bavarian sister party, the Christian Social Union, pushed her into promising tax cuts. Sometimes she hints that fiscal discipline is a higher priority. The CDU's tax-cut proposal is not a pledge of immediate relief but a signal that the party is on the side of the economy's producers, says Viola Neu, a political scientist at the CDU-linked Konrad Adenauer Foundation. Ordinary Germans are not expecting much relief. A majority favours a tax rise as long as it weighs on upper-income earners, according to a recent poll. Oddly, voters may end up electing a government keener on tax cuts than they themselves are.

Economist.com WORLD EUROPE

Dangerous dogs in Denmark

Shoot the puppy!

Aug 20th 2009 | COPENHAGEN
From The Economist print edition

Danes turn on their former best friends

Getty Images

DOGS, not recession or unemployment, are the biggest problem facing Denmark this summer, or so you would think from all the fuss about them. At his Liberal party's summertime get-together on the Faroe Islands, the prime minister, Lars Lokke Rasmussen, solemnly promised a new law to ban aggressive breeds of dog. "We don't want a society", he said with furrowed brow, "where you cannot go walking with your child or your poodle without risking an attack."

Things might seem to be going that way. According to the Danish Kennel Club, the kingdom's population of fighting breeds such as pit-bull terriers, mastiffs and rottweilers has risen from 1,000 to 20,000 in the past five years. The incidence of attacks, mostly on other pets, has grown accordingly. Denmark's national news agency, Ritzau, says there is a violent incident about once a fortnight. Several people have been mauled, though deaths so far have been confined to cats, rabbits and small dogs. Still, widespread worries that the next attack could kill a citizen have pushed man's erstwhile best friend to the top of the political agenda.

However, the prime minister's ringing proclamation was followed by a realisation that a ban on certain breeds—such as Britain introduced—might not work. Fanciers of muscular hounds with big jaws could circumnavigate the law by crossing, say, a mastiff with a pit bull, to create a perfectly legal canine nasty (as, indeed, has happened in Britain).

To meet the difficulty, Flemming Moller, a veterinarian who took over the parliamentary seat vacated when the former prime minister, Anders Fogh Rasmussen, went off to run NATO, proposed a logical, if drastic, solution: kill all mongrels. Mr Moller claims this is the only way to eliminate aggressive traits from the doggy gene pool. Only dogs registered in the national stud book have a record of their parentage and genetic traits. Other puppies, he says, could be the products of anything from joyful encounters in leafy suburbs to deliberate breeding by thugs. With some 40,000 mongrels born in Denmark every year, a mass cull of mutts would reach alarming proportions. Mr Moller is prepared for the backlash: "We will surely see lots of press photos of sweet little puppies being put down but we must be determined," he says unflinchingly.

Happily for the puppies, Mr Moller's idea has won little support. One outraged politician from the junior partner in the coalition, the conservatives, said he would "reach for his shotgun" if Mr Moller came calling. Indignant comments about Nazis and racial cleansing have swamped online forums. All of which leaves the government's attempt to rein in dangerous dogs looking like, well, a dog's dinner.

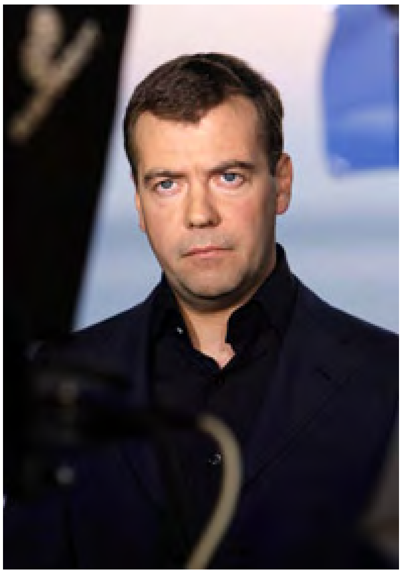
Russia and Ukraine

Dear Viktor, you're dead, love Dmitry

Aug 20th 2009 | KIEV AND MOSCOW
From The Economist print edition

Russia's president writes his Ukrainian counterpart an insulting letter

AFP



Insulting friends and influencing people

RUSSIA marked the first anniversary of its war with Georgia with a verbal salvo against Ukraine. Russia's president, Dmitry Medvedev, wrote Viktor Yushchenko, his Ukrainian counterpart, an open letter with a familiar litany of complaints: Ukraine was supplying arms to Georgia, complicating the life of Russia's Black Sea fleet (which is based in Sebastopol, a Ukrainian port), signing treacherous pipeline deals with the European Union, kicking out Russian diplomats and falsifying joint Soviet history.

Less familiarly, Mr Medvedev posted a special video blog to publicise his letter. Dressed in ominous black, and overlooking the Black Sea with two military boats on the horizon, Mr Medvedev said the Kremlin would not be sending its new ambassador to Kiev.

It took Viktor Yushchenko several days to reply. His response was measured: Ukraine had done nothing illegal towards Georgia; had the right to choose its friends; was entitled to its own view of history and its language; and had repeatedly asked the Kremlin to remove some of its diplomats involved in non-diplomatic work.

But Mr Medvedev was not interested in what Mr Yushchenko had to say. He wanted to register Russia's hand in Ukraine's presidential election due on January 17th. That election is of almost as much importance to Russia as it is to Ukraine itself. In the previous presidential election, Russia backed Viktor Yanukovich, the Russian-friendly prime minister at the time. He lost badly and so did Vladimir Putin, then Russia's president and now prime minister, who had rushed to congratulate him.

The Kremlin fears making the same mistake twice. But this time, in insulting Mr Yushchenko, it is kicking someone who it thinks is certain to lose anyway. It is also laying down rules which it implies the next president must respect if he or she is to be accepted in Moscow. The ability to influence Ukraine's policy is seen by Russia as a test of its resurgence.

To show the range of options for reintegrating Ukraine into its "sphere of privileged interest", Russia recently dispatched Patriarch Kirill, the head of the Russian Orthodox Church, on a tour of Ukraine. "When I walked through huge crowds of people, chanting 'Kirill is our patriarch', I understood that our great spiritual unity …has become a basic value which cannot be shaken by politics," he told a doubtless grateful Mr Medvedev on his return.

As the war in Georgia showed, the Kremlin has other means of persuasion at its disposal. On August 10th, a day before the video blog, Mr Medvedev announced new, simplified rules for using Russian military force outside the country to protect Russian citizens and defend units stationed abroad.

A full-blown military conflict with Ukraine seems unlikely but is no longer unthinkable. (Two years ago a war between Russia and Georgia seemed equally unlikely.) Andrei Illarionov, once an adviser to Mr Putin and now a fierce critic, says the key factor is not whether Russia has the military capacity for a confrontation with Ukraine, but that aggression towards the neighbours has become a way of life for the Kremlin. In the past decade, Russia has managed to alienate almost all the former Soviet republics, even undemocratic Belarus. Trade wars and energy cut-offs have become standard policy responses.

Of all the neighbouring republics, Ukraine remains the largest and most important. As Zbigniew Brzezinski, a Polish-born American national security adviser, once wrote: "Without Ukraine, Russia ceases to be an empire, but with Ukraine, suborned and then subordinated, Russia automatically becomes an empire." It is far from clear, even now, that Russia has fully accepted Ukraine's sovereignty. At a NATO

summit in Bucharest last year Mr Putin reportedly told President George Bush, “You understand, George, that Ukraine is not even a state!”

Unlike Georgia or the Baltic states, which had longer traditions of running their own affairs, Ukraine has had little experience of statehood. “In the last 80 years of the 20th century we declared our independence six times. Five times we lost it,” Mr Yushchenko pointed out in a recent interview.

Ukraine’s politicians and voters seem to be leaving the country vulnerable again. According to a recent poll, more Ukranians think their own government is the biggest security threat to their country than believe Russia is. Corruption and squabbling inside the ruling Orange coalition have paralysed governance. The majority of presidential decrees do not get implemented. Since June Ukraine has not had a defence minister. Its economy contracted by 18% in the second quarter of the year.

“People have lost any respect for their own state,” says Yulia Mostovaya, an influential journalist in Kiev. National ideals have been discredited by cynicism and the corruption of ruling politicians tainted by shady gas deals with Russia. Meanwhile the version of order projected by Russia’s television channels looks increasingly popular (more than 90% of Ukranians say they feel positive about Russia, whereas 42% of Russians see Ukraine as an enemy).

Few leading Ukrainian politicians publicly rebutted Mr Medvedev’s insult to Mr Yushchenko. Most used it as yet another opportunity to kick him. “We have reached a critical point, a point of bifurcation,” says Anatoly Gritsenko, Ms Mostovaya’s husband, a former defence minister and one of the presidential candidates. “Either Ukraine is going down, towards disintegration, or it will start recovering. But the current unstable situation cannot last.”

Russia’s own situation may not be entirely stable and its current rulers may be tempted to provoke a conflict with Ukraine to consolidate their position. One thing looks increasingly certain: the relationship between Russia and Ukraine will be a worry for European security.

Spanish soccer

The drain to Spain

Aug 20th 2009 | MADRID
From The Economist print edition

The Harvard Business School approves of Real Madrid

IT IS kick-off time for European soccer. As national league seasons open across a continent that still manages to attract the world's top talent, eyes are turning to the so-called *galácticos*– the superstars joining Spain's La Liga.

Spain is posting some of Europe's worst GDP numbers, yet summer spending on soccer players has been sky high. Leagues in England, Italy and France have lost out. Portugal's Cristiano Ronaldo, Brazil's Kaká, Sweden's Zlatan Ibrahimovic and France's Karim Benzema have all moved to Spain. They have been greeted by 80,000-strong crowds in rock star-style ceremonies.

One man and one tax regime are responsible. After a disastrous last season coloured by corruption scandals, Real Madrid asked its former president, Florentino Pérez, to take his old job back in June. Mr Pérez wheedled huge loans out of Spanish banks (when the common cry is that credit has dried up) and went shopping. Ronaldo, bought from Manchester United, cost a world-record €94m ($132m). Kaká cost €67m from Italy's AC Milan. They were voted the world's best players over the past two seasons.

Mr Pérez turned Real Madrid into a global brand earlier this decade. He did it by buying the world's most popular stars regardless (some said) of talent. Financially, it worked. They sold merchandise. They brought lucrative advertising and television contracts. The emblem was David Beckham, of England. Real Madrid sold staggering quantities of team jerseys in Britain on the weekend of his signing in 2003. The Pérez way of doing business is a model for clubs in emerging soccer markets such as the United States, Japan and China, says José Luis Nueno, co-author of a Harvard Business School study of Real Madrid.

Income tax also explains Spain's rise. The field is far from flat. Leagues elsewhere must fork out 35-70% more to match the take-home wages of foreign stars in Spain, says Deloitte, a consultancy firm. English fans, whose country is suffering from a weak pound as well as a high top rate of income tax, cry Foul!

Barcelona showed that Spain's growing financial clout is being matched on the field by winning the coveted Europe-wide Champions League last season. England's Premier League remains, however, the world's richest, with revenues of €2.4 billion. Spain, Germany and Italy are €1 billion behind. But England's Premier League spreads its television money wide to create large and medium-sized clubs, whereas Real Madrid and Barcelona grab half La Liga's revenue, creating two sharks in a pool of tiddlers.

Barcelona celebrated by buying Mr Ibrahimovic from Italy's Inter Milan. Its key players, however, are graduates from the club's own training school. They cost little beyond their salaries. Barcelona's triumph spurred arch-rivals Real Madrid into its spending spree. That sets up an interesting clash. Which will win La Liga: cheque-book power, or home-grown talent?

The euro-area economy

Growing apart?

Aug 20th 2009
From The Economist print edition

France and Germany have emerged from recession; Italy and Spain are still struggling. Is the difference between core and periphery a problem?

Illustration by Peter Schrank

ENTHUSIASTS for European integration used to spend a lot of time fretting about a "two-speed Europe" (meaning that some countries would engage in closer integration than others). Now they are fretting about a two-speed euro zone as well.

On August 13th figures showed the euro area's overall GDP had declined by just 0.1% in the three months to the end of June, a much smaller drop than had been expected. The currency zone's two largest economies, France and Germany, both grew by 0.3% in a quarter when many other rich economies, including those of America and Britain, were still shrinking.

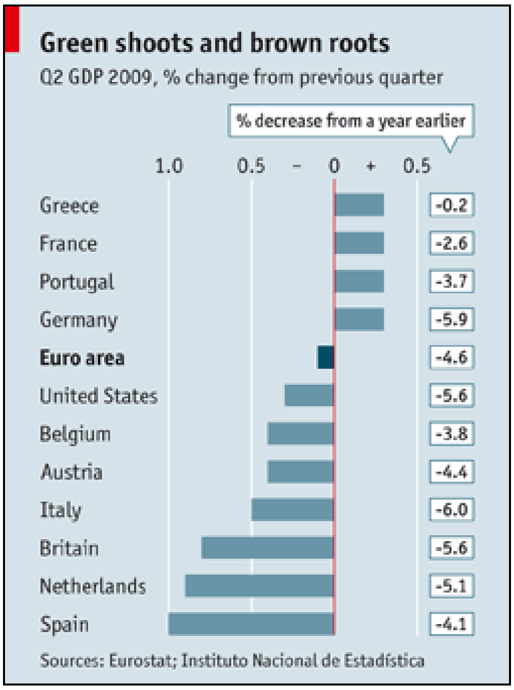
But the region's next largest economies were still mired in recession. Spain's shrank by 1% in the second quarter; Italy's by 0.5%. Analysts reckon this split between a growing north and a struggling south is likely to continue. France and Germany reported that trade boosted their GDPs, suggesting that they are benefiting from the export revival spurred by emerging Asia.

Italy and Spain, meanwhile, look hamstrung by a loss of competitiveness following a long period in which unit wage costs have risen. Italy's exporters of textiles and furniture will find their wares ill-suited to a global rebound dependent partly on Chinese investment spending. And Spain's exporters look puny compared with the large, idle industries, such as construction, that cater to domestic demand.

A closer look at the figures, however, reveals a more complex picture than a simple north-south divide. Northern economies that are very open to trade, such as Belgium, Austria and the Netherlands, were still shrinking in the second quarter, while in the south, Portugal and Greece managed some modest growth (see chart). Look at the slump in the year to the second quarter and the pattern is more uniform, says José Luis Escrivá, at BBVA, a Madrid-based bank. Most economies shrank by 4-5%. Italy did worse, but was underperforming before the crisis. Germany was down by 5.9% or so, owing to its export dependence, but has scope to make up the lost ground as trade rebounds.

The big exception is France, which has suffered far less than most other rich countries. One reason is that it was a bit-part player in the system of global imbalances that precipitated the slump.

France was neither a big supplier of international credit, like Germany or Japan, nor reliant on borrowing, like Spain, Britain or America. In good times, most of the economy's impetus came from within so it was less exposed to trouble from without. Another factor is the French government. When private demand suddenly plunges, it helps to have a well-oiled machinery of state that can quickly step in.



Indeed, the scale and timing of fiscal support explains much of the recent divergence within the euro area. Consumer spending in France and Germany rose in the second quarter, thanks in large part to government subsidies on car purchases. The state in both countries has cushioned consumption indirectly by stemming job losses. In France, make-work schemes in the public sector have kept the jobless rate from rising too far, says Laurence Boone, at Barclays Capital in Paris. In Germany, the accord between industry and government to keep short-time workers on the payrolls has had a similar effect. Spain's fiscal stimulus kicked in earlier so has had less of an impact recently. In Italy, the high level of public debt means the government could not afford much by way of state support.

Germany still has some fiscal stimulus in the pipeline, which may lift its economy above the rest for a while. Its firms were still shedding stocks in the second quarter, as they were in France, so there is scope for a rebound in inventories to spur growth. The increase in export orders should soon translate into higher export sales.

Beyond the second half of this year, however, the scope for France and Germany to pull away from the rest of the euro zone seems more limited. Germany's exporters cannot live off China alone, and their other big customers, in America, Britain, eastern Europe and Spain, will not be as free-spending as they once were. Firms will not carry idle workers for ever. Unemployment is likely to rise in both countries, which will hurt consumer spending. Businesses with better prospects may find it hard to get credit, as long as troubles in Germany's banking system remain unresolved. French exporters have lost market share in recent years, according to analysis by the European Commission. That suggests France is not so well placed to benefit from the revival in global trade.

For now, the euro zone's core countries are likely to do better than those on the periphery. But America and Britain hope to export their way out of trouble, and emerging Asia is slowly shifting towards internal sources of demand. That means the euro zone's economies are likely to have to rely even more on each other in future.

An interview with David Cameron

The man who would be prime minister

Aug 20th 2009
From The Economist print edition

The Conservative leader sets out his thinking to The Economist

PA

OF THE DIARY commitments David Cameron had scheduled either side of his interview with *The Economist* on August 18th, the first, an appearance alongside a feted intellectual at London's Royal Society for the Arts, would enthuse Gordon Brown. The second, a campaign tour, would appeal to Tony Blair. Though he is neither as showily cerebral as the current prime minister nor as scintillating a retail politician as the previous one, Mr Cameron is adept in both settings.

Such roundedness may contribute to the leader of the opposition's lack of definition ("Who is David Cameron?", *The Economist* once asked on its cover). But it also helps to explain why the 42-year-old is the favourite to become prime minister after the general election likely to be held next spring, only nine years since he entered Parliament, and four-and-a-half since he was elected leader of a then reviled Conservative Party. The rapid journey has nevertheless allowed time for disruptive events. Mr Cameron set out to rebrand the Tories as kinder and greener. It worked. The recession and a fiscal deficit he describes as "intimidating" have forced him to re-rebrand them as a party of economic competence and austerity.

Here, his record has been mixed. Mr Cameron insists he was right to oppose the government's fiscal stimulus last year, an initially lonely position that has won adherents since. His critics still invoke his response to the financial crisis in 2007, when he opposed the nationalisation of Northern Rock, a stricken mortgage lender, before eventually bowing to the inevitable. The government did the same, Mr Cameron points out, as if to deny that he allowed right-wing ideology to trump pragmatism. The Tories were also slow to ditch their boom-time pledge to share revenue between tax cuts and public spending. "We should have abandoned Labour's spending plans sooner," he says ruefully.

The main critique of Mr Cameron these days looks to the future. If fiscal retrenchment under the Tories takes the form of spending cuts rather than tax rises (though he does not rule out the latter), where will the axe fall? He has committed to few specific cuts. Indeed, he has declared some areas immune from austerity measures, namely health care, a fraught issue for him of late. On August 13th Daniel Hannan, a high-profile Tory MEP, disparaged Britain's beloved NHS on American television, provoking much ire back home and a slapdown from his leader (see article). Other Tories resent Mr Cameron's commitment to spend more on the NHS but his view "is the one that counts".

If a fiscal squeeze is on its way the Tories will want to win a mandate for it. "Getting the deficit under control will make or break my government," he admits. Accordingly, more fine print will emerge before the election. But by accepting the principle that spending must fall, Mr Cameron says he has already been braver than the government. "I can't think of an opposition party going into an election promising spending cuts since 1929."

Mr Cameron is frustrated at credit not being given where it is due. He and his Treasury spokesman, George Osborne, made a point of resisting right-wing pressure to promise an overall cut in taxation. No one could know the state of public finances in future, they argued during this struggle. Then came the fiscal crisis and, with it, barely acknowledged vindication.

Pressed to say what he has learned from Barack Obama's early travails as American President, Mr Cameron is diplomatically reticent. But he confesses to being wary of having "too many aims and goals". Whatever political capital he can spare from cutting spending will be largely used to introduce market-based reforms to Britain's schools. The plans fit the Tories' theme of "giving power away", which encompasses everything from strengthening local government to *avant-garde* ideas for granting individuals control over the money the state spends on them. Such boldness is missing in other areas, grumble some Tory thinkers.

It is on foreign affairs, however, that Mr Cameron has been most inscrutable. His hostility to further integration of the European Union is clear enough, though he remains vague on what he would do if the Lisbon treaty, which his party loathes, is ratified before the election. Europe may be the least of his worries, though. If troublespots such as Iran, Afghanistan and Pakistan worsen while growth and employment recover at home, international security may begin to rival the economy as the issue of the day at some point during a first-term Tory government. Mr Cameron, against most expectations, may end up becoming a foreign-policy prime minister.

He lists the world leaders he has assiduously cultivated. He mentions his chief of staff, Ed Llewellyn, who brings international contacts from his years as a diplomatic aide. But his efforts to "build a knowledge base" do not signal a direction. His reluctance to "carve out a philosophy" of foreign policy seems wise, as these rarely survive first contact with reality. Instincts and past decisions are a better guide to future action. Mr Cameron's gut feelings on Britain's role in the world may herald a change of direction. Unlike Mr Brown, who seems unmoved by the non-economic aspects of foreign policy, he wants an active Britain on the world stage. (His answer to whether it should punch above its weight is an immediate "yes"). But unlike Mr Blair, he does not insist that the role takes a missionary liberal form.

The right temperament

As for his record, he was sceptical about the Iraq surge and admonished Israel during its war with Lebanon, which cheered his party's doves. They see in William Hague their kind of foreign-affairs spokesman. But Mr Cameron also visited Georgia last year to denounce its invasion by Russia and did not criticise Israel's incursion into Gaza this year—to the delight of Tory neo-conservatives. They may be encouraged that many of his deviations from Blairite orthodoxy (including a speech critical of America on the fifth anniversary of 9/11) took place in his early, rebranding phase as leader. These may have been driven more by the need to soften the Tories' image than by his own sentiments.

The lesson of the Brown premiership, undermined as it often has been by its own obsessive political calculation, may be that temperament is more important to leadership than intellect. If so, Mr Cameron is well-placed. He is whip-smart, to be sure, but the equanimity with which he approaches politics seems the bigger asset during a crisis era. His collegiality ("I like being the chairman of a team") also signals an end to the imperial premierships of recent decades.

Mr Cameron—who has an "implementation unit" devoted to working out how his policies will be put into practice, and a stable if not stellar shadow cabinet—claims to be readier for power than any recent incoming prime minister. But if he is unusually well-prepared, he will also be unusually burdened with challenges.

Transatlantic rift over the NHS

Healthier than thou

Aug 20th 2009
From The Economist print edition

How Britain’s health system compares with America’s

Illustration by David Simonds

THE NHS is the closest thing the English have to a national religion, Nigel Lawson, a former Tory chancellor, once observed. Seldom has that tart comment seemed more apposite than in recent days, as both Gordon Brown and David Cameron leapt to the defence of the NHS following vitriolic criticism in America of Britain’s “Orwellian” health service. Some of the charges against it are absurd, but does the tax-financed NHS deserve such worship this side of the Atlantic?

Comparing the performance of health systems is tricky. For one thing, people may attach different values to crucial features such as coverage, choice, equity and the quality of clinical care. For another, people’s health reflects influences like lifestyles that have little to do with medical care. Cost must also be taken into account. The World Health Organisation attempted an evaluation in 2000, in which Britain came 18th out of 191 countries and America 37th, but the methods used to compile the ranking were heavily criticised and it has not repeated the exercise.

On the most basic metric of life expectancy at birth, Britain (79.1 years) outscores America (77.8). Longevity is admittedly a crude and indirect indicator of population health. Yet a similar story emerged from a study in 2006 that used direct measures to compare the health of middle-aged people: the Americans were sicker than the English.

Another line of inquiry is to investigate how health systems perform in tackling conditions that are treatable, comparing death-rates for such illnesses among the under-75s. Britain does not emerge well from one such ranking, compiled by Ellen Nolte and Martin McKee of the London School of Hygiene and Tropical Medicine. Their study, published in early 2008, placed Britain 16th among 19 advanced countries (France came first). But America came last.

On the other hand, Britain scores worse than America in five-year survival rates for cancer. High-tech diagnostic equipment is less abundant: in 2007 there were, for example, 25.9 MRI scanners per million Americans compared with 8.2 in Britain. Expensive new drugs generally become widely available sooner in America than in Britain. One reason is that in Britain they are subject to a cost-benefit assessment. Although this approach has been demonised in America it merely makes explicit the rationing in any medical system through the decisions of insurers and funders.

And then there’s the question of overall cost. Even after a huge expansion of the NHS budget over the past decade, spending on health care in Britain amounted to 8.4% of GDP in 2007 compared with 16% in America, according to the OECD. Public spending on health care per person is actually higher in America (through Medicare, Medicaid and other government programmes).

Both health systems have their virtues and their faults. At its best, America offers extraordinarily good clinical care, but too many people lack insurance cover or fret about losing it. The NHS provides health care to all at a much lower total cost, but patients have less clout. Both countries are crying out for reforms to bring about better and cheaper care.

Rebuilding Jaguar Land Rover

Tata takes charge

Aug 20th 2009
From The Economist print edition

How a poker game with the government changed the deck at JLR

Alamy

FOR several months, the future of those sleek Jaguar saloons and robust all-terrain Land Rovers, symbols of a once-great British motor industry, seemed to hang in the balance as Tata, parent of Jaguar Land Rover (JLR), and government officials wrangled over the knotty issue of financial support.

Dangling before JLR and other carmakers and suppliers was the promise, made in January by Lord Mandelson, the business secretary, of £2.3 billion ($3.2 billion) of government loans and guarantees to aid investment in low-emission car projects. So far not a penny of the money has been spent, though separately £300m has gone on a car scrappage scheme, which mainly helps makers of small, cheap cars.

On August 11th an exasperated Tata said it no longer needed government help. That ended over six months of sometimes bitter negotiation with the Shareholder Executive, a state agency that looks after the government's stakes in businesses. (Those include Northern Rock, a rescued mortgage bank, but not RBS and Lloyds Banking Group, which are handled by UK Financial Investments.)

Tata, having bought JLR in June 2008 for $2.3 billion, found it was hit by the credit crunch, like all other car firms. Bank funding dried up and in November JLR asked the government for guarantees to enhance its credit on commercial loans. Unlike the French and German governments, which were able to help carmakers via these firms' financing arms, which are authorised banks, the British government did not have that option. The Shareholder Executive had to deal directly with JLR and first of all judge whether Tata, which owns businesses ranging from British steel mills and tea packers, to chemical and car plants in India, was really that needy of cash. Tata's commitment to JLR seemed firm. But JLR had previously been a division of Ford Motor Company: it had no proper treasury function and was thinly capitalised.

In protracted investigations, the Shareholder Executive, staffed mainly by hard-nosed former corporate financiers, began to demand radical changes to JLR's financial structure, if they were to put taxpayers' money at risk. That may have been reasonable, but it was not what Tata management wanted to hear. The European Investment Bank (EIB) was offering JLR a £340m loan for the development of green technology, but required a government guarantee. On top of that JLR wanted around £400m of short-term funding. But the Shareholder Executive played hardball. The requested guarantee shrank to £175m. Moreover, the agency wanted a premium of close to 10% and a counter-guarantee from a commercial bank so that, in the case of a payout, it had a chance to claw back the funds. And it wanted the power to remove JLR's chairman if necessary.

Tata found these terms unacceptable, even an affront, and finally wrote to say it was looking elsewhere: the EIB would get a guarantee from a consortium of banks instead, and JLR would raise bridge finance by pledging future cashflows. This new-found confidence was helped by the buoyancy of Tata's car sales in India, and a modest recovery of orders at JLR.

But there is some residual rancour and speculation that prompter action, at least on the EIB funding, would have accelerated JLR's development of the LRX, a small, low-emission Land Rover, whose production is due to replace that of the Jaguar X-type at Halewood at the end of this year.

On the other hand, it could be argued that abrasive dealings with the Shareholder Executive forced Tata to get to grips with JLR and bring in consultants KPMG to drive down costs, and Roland Berger of Germany to

develop strategy. Ravi Kant, non-executive vice-chairman of Tata Motors, is now spending more time at JLR headquarters in Gaydon, Warwickshire. There are thoughts of more co-operation with Tata, perhaps involving shared production platforms. At the same time Tata does not appear that strapped for cash, having put £1.2 billion into JLR over the past 14 months.

A-level results

Dumbing down: discuss

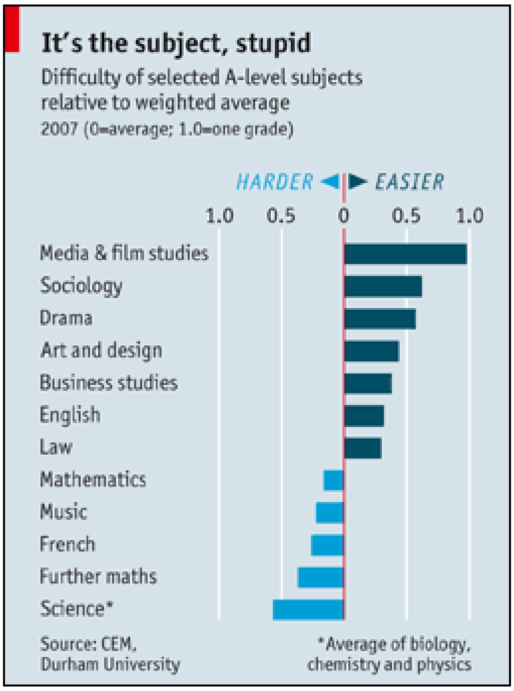
Aug 20th 2009
From The Economist print edition

Answer: the ritual of celebration and hand-wringing will continue

ARE ever-rising A-level results evidence of better teaching and harder-working pupils, as Labour education secretaries claim each August? Or are they proof of spoon-feeding syllabuses and easier exams, as the opposition Conservatives say?

This year's results, published on August 20th, provided another chance for those on both sides to "agree or disagree". The pass rate rose for the 27th year running, and is now 97.5%, up from 68.2% in 1982. The share of A-grades went up too, by 0.8 percentage points compared with last year, and now stands at 26.7%. The end result of this 27-year bull run is that an eighth of all candidates now get three A grades, more than used to get a single A back then.

On the face of it, this is a success story. But probe the figures and they start to look flakier. School league tables, and the less selective universities, count grades regardless of subject, so an A in photography equals one in physics. But that assumption of parity is inaccurate, according to researchers at Durham University. By comparing results in different subjects awarded to the same candidates, and grades at A-level and GCSE, they have shown that some subjects really are softer (see chart). The idea is that an educational "Gresham's Law" is at work, with bad qualifications driving out good as schools push pupils towards easier subjects in the hope of rising up the league tables, and pupils scramble after any old As to present to undiscriminating universities.



There is evidence that this happens—but only at the margins. If the Durham team's figures are used to adjust grades, the real value of newly minted A-levels has fallen a little compared with their face value every year since 2003, as slightly more students choose easier subjects over hard ones than did the year before. During that time a gap of around half a percentage point opened up between the two. The fact that certain subjects are required for many degrees—mathematics for engineering; the sciences for medicine—acts as a countervailing force. So do the selective universities, which generally prefer candidates who take the tougher subjects.

Lacking any such restraint is year-on-year grade inflation across the board. And that, like continental drift, is hard to see in action. One oft-tried way to spot it—looking at old exam papers—is little help, since standards are set more by the marking than the syllabus or test. ("What is love?" is easy if "An emotion" gets full marks; hateful if one must illustrate with sonnets and explain how neurotransmitters function.) But in the long run, it can have a dramatic effect. The Durham team used aptitude tests to show that pupils of a given ability get far higher A-level grades now than they used to 20 years ago. Over the same period an 18-percentage point gap opened up between pass rates in A-levels and the International Baccalaureate.

Alan Smithers, an educationalist at Buckingham University, thinks grades inflate when examiners check scripts that lie on boundaries between grades. Every year some are pushed up but virtually none down, resulting in a subtle year-on-year shift. Wider expectations also seem to be mildly inflationary. He points to 2002, when the cack-handed introduction of a new A-level curriculum led to soaring grades. Exam boards panicked, and shunted grade boundaries to drag them back down. And when results fall, as they did with the English tests taken by 11-year-olds this summer, that provokes outrage too.

The main reform being proposed by Michael Gove, the Tory education spokesman, is for harder subjects like maths to be worth more in school league tables than softer ones like sociology. But since blanket grade inflation rather than a shift to easier ones is the main force at work, this would have little effect. And tackling it would entail limiting the share of candidates allowed to get each grade, as happened until the mid-1980s.

That would be politically tricky, since such limits seem unattractively arbitrary. Moreover, it would mean abandoning any hope of measuring even genuine improvements in educational standards. Whether or not Mr Gove gets the chance to implement his ideas after the next election, the ritual of hurrahs and boos over A-level results seems likely to continue.

Children in prison

Growing up banged up

Aug 20th 2009
From The Economist print edition

Why Britain imprisons so many young people

THE teenagers on their way to Ashfield prison who were made to urinate in plastic bags rather than be let out of the prison-van; the boys at Castington jail who were allowed to shower only twice a week; the seven teenagers at the same prison who suffered wrist-fractures while being restrained by staff: it is easy to hope that, however horrible the details that emerge from official inspections of young offenders' institutions, hardly any young people have to suffer such a fate.

Except, in Britain, that is not the case. Roughly 2.5% of all prisoners in England and Wales are under 18, one of the highest proportions in the rich world (see chart). When one factors in Britain's high rate of total imprisonment, the number of youngsters behind bars is startling. According to figures from the International Centre for Prison Studies at King's College London, Britain locks up a greater proportion of its youth than even America, which leads the world in its imprisonment of adults.

The wayward young can get into trouble at an early age. Last year, under counter-terrorism powers, London's police carried out over 2,000 stop-and-search operations on children under 16 (of whom 58 were under ten). In defiance of repeated urgings from the UN, the age of criminal responsibility in England and Wales is just ten (and in Scotland only eight), lower than anywhere else in Europe, where most countries hold off until 14.

Care is required in comparing these figures: in France, for instance, the age of criminal responsibility is officially 13, but judges can impose educational measures on children as young as ten; in Scotland, with its theoretical minimum age of only eight, few under-16s face adult courts in practice. But the Howard League, a British prison-reform charity, says there is a link between low ages of responsibility and high numbers of children behind bars: Turkey and the Netherlands, which both prosecute children as young as 12, vie with Britain for the biggest proportion of child inmates in Europe.

Younger and younger

Encouragingly, the number of minors being sent to custody in Britain seems to be tailing off: it fell by nearly a fifth between 1997 and 2007. But oddly, within this shrinking group the number of very young children being imprisoned has gone up dramatically. Take 10-14-year-olds: only 130 were jailed in 1997, whereas in 2007 more than 500 were locked up. (Offending rates were broadly the same in each year.) Barnardo's, a children's charity, says the influx of very young prisoners has bumped 15- and 16-year-old inmates up into young offenders' institutions meant for older teenagers.

The most common reason for imprisonment among younger children is the breach of a milder sanction such as an antisocial-behaviour order (ASBO) or curfew. ASBOs are dished out to children for nuisance behaviour that would not ordinarily be jail-worthy, but can lead to custody if breached. Children as young as ten have had such orders imposed on them, leading to extraordinary scenes in court: one Yorkshire boy fell asleep on the bench as the judge handed him his ASBO.

In addition to these new measures, it seems that existing sentencing guidelines are being broken: children aged 14 and under are supposed to be incarcerated only if their offending is both serious and persistent, but Barnardo's found that 35% of children sentenced to custody in 2007-08 did not meet both criteria. The charity blamed unclear definitions of both terms.

Like adult prisoners, child inmates have wretched back-stories: even by the age of 14, a fifth have tried self-harming and almost a tenth have attempted suicide. A big chunk are brought up under the care of the state; those who are not are likely to have grown up in poverty. The deprivation that seems to be at the root of much delinquency will not be helped by the recession: figures released on August 18th showed that the number of young people not in education, employment or training was the highest on record.

Economist.com WORLD BRITAIN

Bagehot

The vanity of ideas

Aug 20th 2009
From The Economist print edition

The Tories' futile quest to find an ideology

Illustration by Steve O'Brien

IN THE political satire "The Thick of It", a character writes a book called "It's The Everything, Stupid". The title captures some politicians' fondness for overarching theories—for ideologies that can coherently and flatteringly explain whatever they are doing, or intend to. Some senior Conservatives are apparently afflicted by this longing. Their theories are not altogether persuasive; but their bigger mistake is to think they need one.

Like schoolboys perpetually re-sitting exams, the Tories—and especially George Osborne, the shadow chancellor—have repeatedly tried to discover an ideology. One contender was "libertarian paternalism", a creed derived in part from the work of American social psychologists and behavioural economists. This seemed to offer a way to unite scepticism of state intrusions with an active interest in social welfare; it suggested that a better society could be achieved by coaxing and swaying citizens rather than compelling them. Alas, it didn't seem to yield much in the way of actual policies.

Then there was a flirtation with "red Toryism", or "communitarian civic conservatism". Its chief prophet is Phillip Blond, head of a new think-tank called ResPublica, who lambasts both state absolutism and atomising liberalism, and believes the Tories must "recapitalise the poor" and "remoralise the market". His thinking combines bits of Disraeli and Edmund Burke with a somewhat fluffy nostalgia. But red Toryism may be too morally censorious, and too hostile to big business, to fit the bill.

The most recent -ism advanced by Mr Osborne and others is "progressive conservatism". This purports to be more than just a bid to irk Labour by pinching one of its favourite adjectives, promising to realise "progressive ends by conservative means". Examples of it in action are said to include plans to devolve power to local councils and to use the internet a lot. Mr Osborne also adduces proposed reforms to health care and schools which, he claims, would both improve provision and save cash. But some Tory policies, such as tax support for marriage, can scarcely be described as progressive even under the most generous definition; and progressive conservatism has sometimes looked like rhetorical camouflage for old-fashioned belt-tightening.

These assorted oxymorons have some common features. They are responses to Tory unease about the impact of the financial crisis on the party's intellectual foundations and the government budget. In a bid to redefine Conservatism, each looks back to traditional models that mix paternalism with a preference for a

smaller state. And none is very convincing.

If the Tories are to be judged on whether they have a theory of everything, they look like failing the test. Fortunately for them, they won't be. So the real question is not over the tenets of their political religion, but why some Tories are so keen to find one.

Brains v balls

Asked about the purpose of ideologies, some politicians cite the importance of impressing journalists, those suggestible traders in second-hand ideas. Ideologies are also said to provide a helpful steer to the civil service about a government's direction. Some claim a credo can help to galvanise an electorate bored by consensual centrism. In tough economic times, fans of ideology argue, it can help to explain change and maintain social cohesion.

Perhaps. But what Britain wants from the Conservatives is a sense that they can yank it out of the economic and fiscal hole it has sunk into. Gut feeling tells many Britons the Tories are best-suited to this job. But the hunch is more emotional than ideological—indeed, the thought that the drastic public-spending cuts a Tory government might make were motivated by doctrinaire conviction, rather than necessity, would diminish the party's appeal rather than enhance it. The Tories need a clear goal and a map for reaching it; they need fresh ideas about the role of the state. But a set of ideas is not the same as an ideology.

The Tory party, in fact, has for most of its history succeeded by eschewing systems and managing not to believe too strenuously in anything. It has a serviceable set of prejudices, for sound money, national sovereignty, self-reliance and so on. But it has survived and flourished by swallowing hypocrisies and reversing positions to win and keep power. David Cameron, the Tory leader, who has prospered by adapting his views and political persona (and who sounds more sceptical of all-encompassing doctrines than some of his colleagues) is himself an example of this talent. In general, in Britain, the left has relied on visions of Utopia to get elected; the right has offered to run the place better.

Probably the main factor that has obscured this rule is the vain urge of some Tories to think of themselves as philosopher-kings rather than mere technocrats. That yen derives from a misreading of two leaders whom today's Conservatives view with a kind of Oedipal awe: Tony Blair and Margaret Thatcher. In opposition Mr Blair's team developed the concept of the "stakeholder society" and the grandiose "third way", which avowedly reconciled market economics with social democracy. Mrs Thatcher harvested ideas from radical think-tanks and continental intellectuals. But, for both leaders, theory served mostly to rationalise their instincts. The "third way" was as much a description of the political realities of the 1990s as a manifesto. Mrs Thatcher started with a notion of Britain and only retroactively found it validated by Hayek and Bastiat. She was much more of a pragmatist than is often credited; it was when she ditched that approach to pursue the Platonic ideal of Thatcherism that she was undone.

The Tories should stop worrying about whether their view of the world works in theory, and concentrate more on generating ideas that will work in practice. They can live without an ideology; what they urgently require is balls.

Piracy and private enterprise

Splashing, and clashing, in murky waters

Aug 20th 2009
From The Economist print edition

Private security firms are increasingly involved in the fight against pirates. The allocation of tasks between them and navies needs some thought

EPA

OF THE dozens of ships recently captured by pirates off east Africa, few stirred so much interest in their home country as a German freighter, the *Hansa Stavanger*, seized by Somalis in April. As its captivity wore on, the crew of 24 was reported in Germany's media to be ailing and in need of medicine and water.

At one point, German police commandos were training on board an American navy ship, hoping to storm the vessel, until America's national security adviser, James Jones, said it was too dangerous. At last, on August 3rd, the saga ended after negotiations between the ship's Hamburg-based owners and the pirates, who boasted that they had netted $2.75m in ransom.

Parleying with pirates, and then paying the ransom (often by airdrops), are jobs that shipowners regularly contract out to private firms or "risk consultancies". Other maritime security services are less controversial: fitting ships with kit, such as barbed or electric wires, to make it hard for pirates to clamber aboard. Increasingly, security firms also put armed guards on ships, or offer their own craft as escorts.

Business protecting ships off east Africa has tripled in the past year, says Eos Risk Management, a London firm that says it has fended off at least 15 attacks from Somali pirates since January. Eos usually uses non-lethal defences, but David Johnson, its boss, says new players are rushing into maritime security, taking advantage of the ample supply of weapons in Africa.

Armed escort ships, offering protection for a price, are becoming a lot more common off east Africa. Local coastguards, where they exist, have got used to private-security vessels plying their waters, says Stan Ayscue of Securewest International, a firm based in Singapore and Virginia.

But for strategists grappling with the diminished safety of the world's seas—off east Africa and in other perilous spots such as South-East Asia and the waters of Nigeria—figuring out a sensible and workable division of labour between navies and private firms is not easy.

In at least one way, the activities of private firms clash with the concerns of navies and their masters. The payment of ransoms is a menace for law and order. As Robert Gates, America's defence secretary, lamented in April, the fight against piracy would be going better if shipowners stopped paying to regain their vessels.

But of course, when private security companies, often employing veterans of national armed forces, work well to prevent piracy, they and the world's navies are broadly on the same side. America in particular says countering piracy requires a joint effort by states, shipowners and other private interests, including security firms. "In appropriate circumstances, onboard armed security, private or military, can provide an effective deterrent to pirates in the Horn of Africa region for certain vessels deemed to be at high risk," the State Department has said.

It is clearly true that no single agency in the war against piracy is likely to succeed. About 15 countries conduct anti-piracy naval patrols in the Indian Ocean under various hats. That might sound a lot; but 30 warships are operating in an area almost as big as the United States. Achim Winkler, a spokesman for the European Union naval force, says hundreds of ships would be needed to secure the area.

And for navies, almost as much as for private security providers, the surge in piracy has affected their institutional interests in confusing ways. As cynics note, the fight against piracy has certainly given navies a noble new mission, a claim on budgets and an area for cross-border work to which nobody objects.

NATO's new secretary-general, Anders Fogh Rasmussen, recently agreed with Russia's envoy to the alliance, Dmitry Rogozin, that piracy was a field where they could work together. However, Russia, which has sent a series of naval ships to the Horn of Africa, says it will not serve under NATO or EU command.

Meanwhile, the Russian navy has in recent days been engaged in what it has presented as a dramatic anti-piracy mission: apprehending, off the Cape Verde islands, eight people on board a Russian-owned cargo ship called the *Arctic Sea*, whose crew claimed to have been hijacked, at least briefly, in the Baltic in late July. Other countries were sceptical of that story.

Apart from biggish powers like Russia, the war on piracy is attracting small countries. For example, Croatia recently said it was joining an EU-led force, after vowing to respect the "human rights" of pirates.

John Pike, of GlobalSecurity.org, an American consultancy, offers a hard-boiled view of all this. "A lot of navies are looking for something to do—and there are many ships in the world prepared for big naval war, which isn't going to happen."

But some naval types say tackling barefoot Somalis with bazookas is not the best use of large warships. “They feel that tackling a skiff is an odd thing to do with a ship costing hundreds of millions,” says Jason Alderwick, an analyst with the London-based International Institute for Strategic Studies. Nor are warships always ideal for the job. A naval craft may take 20 minutes to send a helicopter to a nearby merchant vessel in danger. That is easily enough time for pirates to seize a ship; once that happens, there is no easy way to regain control.

Deterrence, or at least stopping attacks at the earliest stage, is always best. These are areas in which the private sector (both shipowners and their security advisers) must play a role. America has also encouraged small countries with large shipping registries such as Liberia, Panama, the Marshall Islands and the Bahamas to mandate prudent self-protection by vessels.

Already, the line between peaceful merchant ships and naval ones is blurring a little. These days, maritime-security providers operating off east Africa almost always make some use of weapons, says Didier Berra, a French army veteran who has worked for Secopex, a naval-security firm based in Carcassonne in France.

Draconian force is seldom necessary, adds Mr Berra. Attackers often give up when 12.7mm machineguns are fired into the water, creating a big splash. The head of another European security firm says many outfits sidestep bans on weapons in port by tossing them overboard. Yet a show of firepower is increasingly necessary because pirates are getting blasé about “non-lethal” defences like water hoses and sonic blasts, says David Schewitz, whose California-based company, RSB International, helps protect ships.

Navies are also starting to deploy seamen on merchant ships, something hitherto rare unless the cargo was military. The French navy, for example, has been sending sailors to protect the country’s tuna-fishing ships in waters around the Seychelles. Such assertiveness at least marginally reduces the opportunities for private firms; a few games really are zero sum.

In any case, private security firms can’t do more than tackle the symptoms of piracy. More needs to be done onshore. Tracking where the ransoms are stashed, reportedly in banks in the Gulf, would be one way to start. Another idea would be to find new ways for young Somali boat-owners to survive. Somalis who once fished say they were pushed out by foreign trawlers.

Ultimately piracy in Somalia is unlikely to stop until chronic instability, caused by rival warlords and Islamist fighters, is tackled. Yet no outsider has a convincing panacea. American forces have bombed Islamist fighters in southern Somalia, and Russia favours knocking out pirate coastal bases; neither action promises stability.

The absence of an effective state in Somalia means there is no local ability to police national waters. Last year the “transitional federal government” signed a deal with Secopex under which the firm would have set up a small national navy. Secopex estimated it would need two dozen fast gunships. But the deal failed. The government was too broke and disorganised.

Across Africa, in Nigeria, lies another danger zone for ships. According to GEOS, a French firm, the insurgents who make pirate-like attacks on shipping in Nigeria’s Delta region are very well armed and informed about targets, through contacts in the oil and shipping worlds. Yet Nigeria’s semi-functioning state helps keep piracy within bounds. GEOS typically protects its clients’ ships with help from a Nigerian police boat or small navy gunship.

The UN Security Council has authorised naval ships to enter Somali waters in pursuit of pirates. But the high seas are simply getting more perilous than they were, and neither governments nor private interests seem to have the capacity to make them safe.

The Lockerbie decision

A long shadow

Aug 20th 2009
From The Economist print edition

A controversial decision to release a Libyan prisoner

Reuters

The quality of mercy

THE bombing that blew up Pan Am flight 103 in the sky above Lockerbie, a small Scottish town, on December 21st 1988, was the worst terrorist atrocity in British history. Of the 270 people who died, 189 were Americans; 11 were killed on the ground by falling debris. On August 20th the only person convicted of the crime was released from prison in Scotland.

After a tortuous diplomatic and legal process, Abdelbaset al-Megrahi, a Libyan intelligence agent, was tried in the Netherlands, but under Scottish law, in 2000-01. His co-accused was acquitted; Mr Megrahi was sentenced to life, with a minimum term that was later set at 27 years. Now suffering from advanced and terminal cancer, Mr Megrahi had asked to be released on compassionate grounds. Separately, under a prisoner-transfer agreement that they recently agreed with Britain, the Libyan authorities requested in May that he be sent home to serve out the rest of his sentence.

Under Scotland's devolution settlement, a little improbably the man responsible for deciding Mr Megrahi's fate was Kenny MacAskill, the Scottish justice secretary. Mr MacAskill, had three options: release (as sanctioned by a Scottish law of 1993); transfer; or keep Mr Megrahi in Greenock prison for his few remaining days. Mr MacAskill rejected the transfer request, managing several digs at the British government as he did so. But he approved the compassionate release; there was talk of the prisoner being whisked back to Libya in a jet sent by Muammar Qaddafi, the country's erratic leader.

Many Americans vociferously opposed sending Mr Megrahi back. In unusually strident language, Hillary Clinton, the secretary of state, said it would be "absolutely wrong" to free him. Ted Kennedy, John Kerry and others also weighed in. So did some relatives of the dead.

But others, including some relatives of British victims, will be disappointed for a different reason. There are lingering questions about Mr Megrahi's role and those of other individuals and states. (In return for the lifting of sanctions, Libya compensated the families of the dead and acknowledged responsibility for the bombing—thought by some to be retaliation for the 1986 American air strike on Tripoli—but Libyan officials implied the move was motivated by pragmatism rather than guilt.) The Scottish Criminal Cases Review Commission, which investigates potential miscarriages of justice, had referred the case for a second appeal. But to be eligible for transfer, on August 18th Mr Megrahi dropped this appeal. So the evidence will now not be re-examined in court.

Alex Salmond, Scotland's first minister, insisted before Mr MacAskill's decision was announced that "there will be no consideration of international power politics or anything else." But the Lockerbie case has always been intertwined with high politics, in particular with Mr Qaddafi's efforts to launder his reputation and drag Libya out of international isolation. His country's rich hydrocarbon deposits and its role in the fight against Islamist terrorism may also be considerations. The fact that his son recently bumped into Lord Mandelson, Britain's powerful first secretary, on holiday in Corfu, has fuelled speculation about a stitch-up. Whether or not such chatter is overheated, and whatever the demands of compassion, justice seems not to have been well-served.

Economist.com **BUSINESS**

Consumer goods in the recession

The game has changed

Aug 20th 2009 | NEW YORK
From The Economist print edition

The recession has spelt disaster for most brands of packaged goods, but not all

Getty Images

JUST last year, when Alan Lafley, the boss at the time of Procter & Gamble (P&G) released his book "The Game-Changer: How You Can Drive Revenue and Profit Growth With Innovation", readers flocked to understand the business strategy of the world's largest consumer-goods firm, then worshipped as a paragon of strong management and profitability. Now, however, the company is confronting a game-changer that Mr Lafley had not foreseen: a global economic downturn.

Earlier this month P&G reported profits of $2.5 billion, down 18% in the most recent quarter from a year earlier. Sales of its products—which include such brands as Bounty paper towels and Tide detergent—were down 11%. Analysts worry that it might take years for the company to restore its profits to their former levels.

For most packaged-goods firms, recent earnings reports were grim. Unilever, the world's third-largest consumer-goods firm by sales, announced this month that profits in the second quarter were down 17% from a year ago. Kimberly-Clark, the maker of Kleenex tissues and Scott paper towels, Sara Lee, a manufacturer of frozen foods, and Colgate-Palmolive, with its eponymous toothpaste and soap, all saw revenues drop in the past quarter. Firms that specialise in food, including Nestlé, Kraft and Kellogg, are holding up better than those that sell products for cleaning and grooming, but only because consumers are preparing more meals at home.

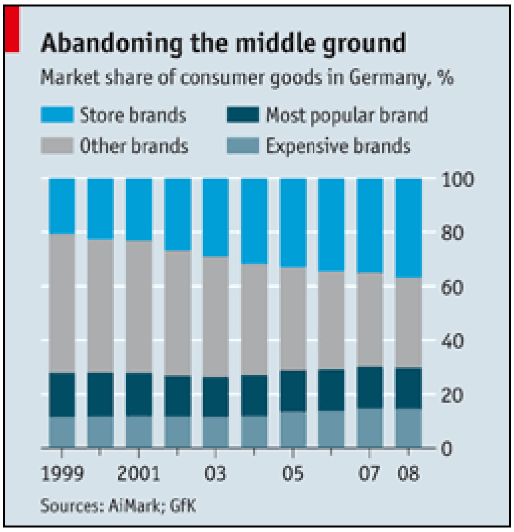
Consumer goods were once believed to be as recession-proof as any industry can be. Shoppers might not be able to afford Rolex watches and champagne during a downturn, the theory ran, but everyone still needs staples such as soap and toilet paper. Yet sales have fallen in this downturn, thanks largely to growing competition from stores' own brands, or "private labels". Private-label goods tend to cost about a quarter less than branded ones, and so appeal to penny-pinching consumers. Some shoppers are also forgoing altogether items that they used to consider staples, such as air fresheners or special detergents for sensitive skin. The big brands' recent, ill-timed price hikes of as much as a fifth in response to rising commodity prices have accelerated the trend.

Retailers have also been giving more shelf space to their own products, on which they earn better margins, further squeezing the big brands by making them less visible. Jan-Benedict Steenkamp, a marketing expert at the University of North Carolina, estimates that the share of private-label goods is

now 20% at Wal-Mart and 35% at Kroger, two huge American retailers.

In the past year private-label sales have grown by around 9% in America and 5% in Europe, gaining market share from branded goods in many categories. Middle-market brands, measured by price or sales, are particularly vulnerable to competition from private labels; even in countries like Germany, where private labels now account for almost 40% of sales, the best-selling and most expensive brands have not lost much ground (see chart).

Many analysts believe that the flight to private labels will outlast the downturn. Ali Dibadj of Sanford C. Bernstein, a research firm, estimates that about half the people who have recently switched to private labels will never go back. The quality of private-label goods has improved, making it harder for consumers to discern any difference between a store's brand and a more expensive rival, particularly for commodities such as paper towels or milk.



Yet not all consumer-goods firms have succumbed to the onslaught of the private label. Reckitt Benckiser, a medium-sized British firm, reported a 14% increase in profits in the second quarter compared with the previous year, and an 8% increase in sales. The firm, which is the world's biggest manufacturer of household cleaning supplies, such as Lysol disinfectants and Spray 'n Wash stain remover, has raised its sales and profit targets for the year, whereas P&G has reduced them and Unilever has scrapped them altogether. This was not just a lucky quarter. While Reckitt's net revenue grew by 9% between 2005 and 2008, P&G's was up only 5% and Unilever's 6%.

Reckitt puts its success down to management, marketing and the positioning of its brands. Its hierarchy is surprisingly shallow: there are only one or two managers between the chief executive and his regional marketing officers. This allows the firm to make decisions more quickly than its competitors, says Bart Becht, Reckitt's boss. The firm can turn ideas into goods on shelves in around nine months, at least three months faster than its rivals.

Mr Becht insists that consumers can still be persuaded to pay for more expensive, branded goods. Reckitt increased its spending on marketing by 25% last year, when most of its competitors were cutting back. The firm takes pains to cater to all budgets. It sells four versions of its Finish dishwashing detergent, for example, at different prices. (The latest and most expensive version of Finish, called "Finish Quantum", costs more than twice as much as the most basic variety.) Reckitt is still adding extra frills to its goods, and pricing them accordingly. It recently released a new air freshener with a motion sensor to tell it when to spray its perfume, which is a fifth more expensive than the humbler sort, for example. Mr Becht says consumers will not pay for minor alterations, such as new flavours and scents, but they will for more significant innovations. "We've proven that in a downturn, consumers don't walk away from better products," he says.

This is a very different strategy from that of Reckitt's rivals, which, after years of sprucing up their products and pushing up their prices, are scrambling to introduce cheaper options. P&G, which has one of the most high-end brand portfolios of any of the packaged-goods firms, has tried to attract customers by launching "basic" versions of its popular brands. It recently released Tide Basic, which costs around a fifth less than its more upmarket cousin. But taking an existing brand downmarket in this way can be dangerous, analysts say. Consumers are unlikely to revert to the more expensive version if they are offered a similar product for less.

Unilever, P&G and others are also cutting their prices and increasing sizes to compete with private labels—although that can obviously cut into profits. Targeted advertising, which directly compares the quality of a branded product with a private-label rival, is also a short-term solution for consumer-goods companies, which are keen to remind their customers why paying more is a good idea.

The worst of the pressure on consumer-goods firms should dissipate when the recession ends. But if the pessimists are correct, and a good number of Western consumers stick to the frugal habits they have learned in recent months, branded products will continue to suffer. One way to revive growth will be to place a greater emphasis on emerging markets in Asia and Latin America, where private labels are unlikely to take hold in the near term, since retailers are smaller and do not have the knowledge or resources to produce their own brands. In that regard Unilever, which already gets over half its revenue

from emerging markets, is better positioned than P&G.

Another strategy would be to sidestep retailers completely and sell directly to consumers through the internet. P&G's new boss, Bob McDonald, has alluded to this sort of plan. It could be exactly the type of "game-changer" his company desperately needs.

Reader's Digest declares bankruptcy

Unsexy and unsuccessful

Aug 20th 2009
From The Economist print edition

How a once-mighty publisher fell, and why it may rise again

Getty Images

A purpose-driven purchase

A FEW years ago it was feared that the investors scooping up one media company after another and loading them with debt would ruin their purchases. As it turns out, some have also ruined themselves. On August 17th the Reader’s Digest Association, publisher of America’s most widely read magazine, said it would seek bankruptcy protection to restructure $2.2 billion in debt. The consortium that bought the company two years ago, led by Ripplewood Holdings, a private-equity firm, would lose its investment under the plan. The future of Reader’s Digest, by contrast, looks brighter.

These days Reader’s Digest is a global business: it generates less than half of its revenue in America. Most of its money comes from direct marketing (that is, junk mail) and sales of things as varied as wine, vitamins and books. It also runs Allrecipes.com, a popular website. But the corporate brand is built on the magazine, and the company has not been helped by its epic decline.

Reader’s Digest began in the 1920s by summarising books and “articles of lasting interest” from other publications. Gradually it acquired its own editorial voice, and with it a somewhat stodgy image. The magazine emphasised homespun values and leaned to the right—Richard Nixon and Ronald Reagan were fans. In the 1970s it sold as many as 18m copies a month. The *Wall Street Journal* described it as the greatest publishing success since the Bible.

Yet cracks were appearing. The magazine came to depend on competitions and sweepstakes, particularly to lure younger subscribers. Forced out of that business by public and legal pressure, *Reader’s Digest* attempted to reinvent itself as a celebrity-heavy lifestyle magazine. Despite heroic (and expensive) efforts to keep up the numbers, circulation has fallen relentlessly. It now stands at 8.2m in America—not many more than *Better Homes and Gardens*.

These days *Reader’s Digest* is aiming for a circulation of about 5.5m, having dropped the notion of being all things to all readers. Instead it will emphasise the heartland values of family and practicality. Other initiatives point in a similar direction. In 2006 the firm successfully launched a magazine featuring Rachael Ray, a cheerful and uncomplicated television cook. Earlier this year it formed a publishing alliance with Rick Warren, an evangelical pastor whose book, “The Purpose-Driven Life”, has a more plausible claim to be the greatest publishing success since the Bible. Mr Warren is conservative but pointedly non-political.

This is wise. There are a lot of people in the heartland, and not just in America. Reader’s Digest’s talent for distilling complex arguments ought to be more valuable in an era of information overload. In the past year *Every Day with Rachael Ray* and the American edition of *Reader’s Digest* have lost less than a tenth of their advertising pages, according to *Mediaweek*—far less than the competition. If it can escape that troublesome debt, the least sexy of publishing companies ought to be around for a while yet.

Economist.com BUSINESS

Copyrights and wrongs

Aug 20th 2009 | SYDNEY
From The Economist print edition

Literature and commerce do battle Down Under

Eyevine

Peter Carey, a literary patriot abroad

THE most talked-about book in Australia at present is "The Slap", a novel by Christos Tsiolkas, a Greek-Australian author, about the consequences of the disciplining of a child at a suburban barbecue by someone other than his parents. Its setting is emphatically antipodean and so, too, are its voices: eight characters drawn from Melbourne's polyglot middle classes. It is precisely the kind of work that the Australian publishing industry claims will be endangered by what, in literary circles at least, is Australia's most talked-about policy proposal: a recommendation being considered by the government to eliminate "territorial copyright".

Under Australia's copyright laws, local publishers have 30 days to produce their own editions of books published elsewhere. If they do so, local bookstores must sell those, rather than foreign ones. But local editions, says the Productivity Commission, the government's economic think-tank, are about 35% more expensive than foreign ones. Consumers end up bearing this extra cost. The novels of Peter Carey, the country's most acclaimed contemporary author, are cheaper in America (where he now lives) than in Australia, laments the Productivity Commission. It is therefore urging the government to amend the law.

Yet the opponents of the proposal—a "Who's Who" of Australian literature—argue that novelists like Mr Carey would never have been published had it not been for territorial copyright. As the Booker-prize-winning novelist himself pointed out to the Productivity Commission, "My writing life has been made possible by the Australian publishers who accepted my work when it was rejected in London and New York, who believed in a literature that would define Australia for Australians and represent us to the world." The flourishing publishing industry makes no apology for resorting to this kind of cultural nationalism. It fears a return to the days when Australia was a "colonial depot" for unsold books from Britain. Australian publishers could "simply become distributors in a global supply chain", according to Mr Carey.

In response, the Productivity Commission has suggested that the young, aspiring Peter Careys of the future might be succoured by government grants. It notes, as well, that territorial copyright protects all titles equally, and thus does not differentiate between books of high cultural value and those of questionable worth.

The Coalition for Cheaper Books may lack Mr Carey's erudition, but it does have a ringing slogan: "Wider reading through cheaper books". Set up by Dymocks, a leading bookstore chain, and the big supermarkets, the coalition also has commercial and political clout. It claims that territorial copyright is not only anachronistic but unsustainable in the internet age. After all, many Australians already bypass the restrictions on foreign editions by importing books themselves, using online stores such as Amazon. Even with the shipping costs to faraway Australia, that is often cheaper than buying locally.

Ultimately the decision rests with Kevin Rudd, Australia's prime minister, a bookish type who famously penned a 7,000-word essay for a highbrow magazine, the *Monthly*, warning against "free-market fundamentalism" and "extreme capitalism". Then again, he also likes to rail against high prices with populist fervour.

Most of the English-speaking world, including America, Britain and Canada, still retains territorial copyright. The main exception is New Zealand, which gave it up in 1998. Different studies have pointed to different effects, from the earlier release of new titles to a flood of cheap foreign children's books. In 2004

a report found that local publishers were producing a narrower range of titles, with an emphasis on rugby and images of New Zealand's idyllic countryside. That is exactly the sort of blow predicted by authors and publishers of books like the "The Slap".

Volkswagen and Porsche

My other car firm's a Porsche

Aug 20th 2009
From The Economist print edition

Despite a distracting merger, Germany's biggest carmaker is doing well

THE feud between Porsche and Volkswagen, and between the Piëch and Porsche families that own most of them, had dragged on for two years. First, tiny Porsche, which makes 100,000 cars a year, tried to take control of VW, Europe's biggest carmaker, which makes 6m a year. But the sports-car firm buckled under the debts it acquired along with 51% of VW's shares and options to buy yet more. Then VW tried to take over Porsche, but that deal also stalled until Porsche's boss and finance chief resigned last month.

Now the two companies, with the help of one of Qatar's sovereign-wealth funds, have at last laid out a road map for a merger by 2011 at the latest. Many of the details are still rather vague, especially regarding the Qatari investment, but there is no longer any argument about where the two companies are heading.

VW is buying 42% of Porsche for €3.3 billion ($4.7 billion). It will pay as much again for a big car dealership Porsche owns, which may be sold later to shore up the merged firm's finances. VW will also raise up to €4 billion in new capital to fund the purchase, in order to keep its balance sheet strong and hold on to its solid credit rating. Qatar Holding will buy 10% of Porsche, plus most of its options to buy VW shares. Later, VW's management says, the two carmakers will merge fully, with the two families owning some 40% of the new entity, the German state of Lower Saxony 20% and Qatar Holding slightly less than that. Barely a fifth of the shares will float freely.

VW's shares have gyrated wildly since the deal was announced on August 13th, as investors tried to work out who would buy what, when and at what price. At one point they fell by nearly 16%, hinting at fears that VW is paying too much to fold Porsche into its large stable of brands.

But VW, which has been one of the few carmakers to hold its own as markets collapsed, claims that closer integration from shared design and pooled purchasing will, in the long term, boost the merged firm's operating profit by €700m a year. The enlarged VW will have eight passenger-car brands, plus bus and truck units.

The underlying strength of the VW group is that it manages to make a range of models that appeal to different segments of the market but use many of the same parts, especially in the bits of vehicles that are normally out of sight. Although this "platform" strategy is now commonplace within the industry, VW has adopted it without eating into sales of more expensive models. The Skoda Octavia is built from the same basic parts as the more expensive VW Golf, but finish, add-ons and marketing have made both models successful in their respective slots. Until now the only collaboration between VW and Porsche has been the Porsche Cayenne, which is a luxury version of the Touareg, a sport-utility vehicle made by VW. As the two companies get closer, Porsche's technology could boost the appeal of VW's more expensive models.

In Europe the VW brand alone outsells all others, with sales in the first six months of the year of 973,000, ahead of Ford with 793,000, according to JATO Dynamics, a research firm. Sales in Europe of VW's star model, the Golf, have risen nearly 16% so far this year, making it Europe's bestselling car, ahead of the Ford Fiesta.

A strong performance in China and Germany (boosted by scrappage schemes in both places) helped VW increase worldwide sales by 7% in July compared with a year earlier, its third monthly increase in a row. But the group's global sales are still down about 4% so far this year compared with the first seven months of last year, though that is much better than the average for the industry. In Brazil, a relatively buoyant market, VW is vying with Fiat to become the market leader.

If the Porsche merger goes according to plan, a resurgent VW could soon be challenging Toyota for the title of the world's biggest carmaker. VW's managers would doubtless welcome the chance to get on with building cars, and put all the financial engineering behind them.

Competition comes to Mexican telecoms

Talking and saving

Aug 20th 2009 | MEXICO CITY
From The Economist print edition

Mexico's dominant telephone firms are under attack

Alamy

It's getting cheaper

AFTER years of exorbitant telephone prices, Mexico's beleaguered consumers are finally getting a reprieve. Local fixed-line calls now cost a flat 1.5 pesos ($0.12) if billed individually, regardless of duration, similar to prices elsewhere in Latin America. Mexico's mobile-phone rates are the third-cheapest among Latin America's big economies at current exchange rates. All this has come despite the near-monopoly enjoyed by firms controlled by Carlos Slim, Mexico's richest man: Telmex, which operates 92% of the country's fixed lines, and Telcel, which controls 72% of its mobile market.

The national antitrust commission cannot curb Telmex directly because it lost a bid to declare the company a "dominant" player in 2007 after a decade-long court battle. (The judge ruled that the government had not amassed sufficient proof of the company's market power, prompting the commission to file a new claim last year.) Telmex has been equally successful at fending off attempts to grant rival companies access to its network of copper wires, which serve 18m customers.

But technological trends, foreign competition and the global recession have rapidly replaced Mr Slim's lawyers as the most important factors in Mexico's telecommunications industry. Ever since regulators instituted a "calling party pays" system in 1999, whereby mobile customers receive calls free of charge, fixed-line service in the country has stagnated while mobile traffic has grown ninefold.

Telmex's business has been further weakened by the emergence of "triple play" providers which offer phone, internet and television by cable. (Regulators have been allowed to bar Telmex from offering television, in an effort to foster competition.) As a result Telmex's fixed-line revenues have fallen from 27 billion pesos in the second quarter of 2007 to 21 billion pesos in the same period this year.

Of course, the biggest beneficiary of the explosion in mobile-phone traffic has been Mr Slim. Telcel came to dominate the local market by pioneering pre-paid billing and investing in coverage all across the country. But Telcel faces much greater competitive pressure in the mobile market than Telmex does in fixed lines.

Since 2006 competition in the Mexican mobile market has been stiff. Movistar, owned by Spain's Telefónica, has increased its market share from 14% to 20% by aggressively subsidising handsets and courting business users with cheap plans. The upstart now signs up nearly a third of new clients, and after years of losses it is finally profitable. Regulators have reduced prices further by cutting the fees charged to connect calls between competing networks by 10% a year. And Telcel itself has cut rates in order to attract poorer customers, who are more frugal than ever because of the country's plummeting economy. As a result, Mexican mobile costs have fallen by three-quarters in real terms over the past seven years.

Many anti-competitive rules remain in place. Regulators continue to set stiff fees on calls between fixed lines and mobiles, which hurts Telmex less than its rivals. A Byzantine map of charging zones means that calls spanning just a few miles are often billed at long-distance rates. And calls to Mexico's poorer and more remote regions, where Telmex retains an absolute monopoly, remain expensive.

Mexico's telecoms infrastructure is also rickety, in part because uncertain regulations have put off potential investors. From 1998 to 2007 the country received just 21% of Latin America's telecommunications investment, despite accounting for 31% of the region's output. Only 22% of the population has access to the internet, compared with 35% of Brazilians. Most of its "broadband"

connections would not be considered worthy of the name elsewhere.

Fortunately, a partial solution for many of these problems is likely to emerge soon. Running alongside the country's intercity power lines is a bundle of fibre-optic cables, which were originally installed to monitor the electrical grid's performance. Earlier this year the government announced plans to sell access to some of these cables, a move that should greatly reduce long-distance rates in much of the country. It is also expected to improve internet access dramatically: Jean Paul Broc, the boss of the triple-play firm Cablevisión, estimates that the new fibres could reduce the cost of bandwidth in Mexico's southeast by two-thirds.

There is still plenty of room for prices to drop further, given that Telcel's profit margin last year was an astonishing 52%. If the regulators get their way, Mexico's callers will soon be happier still.

Cathay Pacific, Air China and Citic Pacific

Landing rights

Aug 20th 2009 | HONG KONG
From The Economist print edition

An airline deal signals a shift in China's approach to investments abroad

Illustration by Claudio Munoz

ON THE face of things it looks like a small deal: on August 17th Air China, China's flag carrier, announced it was raising its stake in Cathay Pacific, Hong Kong's biggest airline, from 17.5% to almost 30%. But the kind of incremental shift in share ownership that would signify little at a Western firm can speak volumes when Chinese state-owned firms are involved.

The four parties to the deal, including Citic Pacific, which is selling the shares, and Swire Pacific, the conglomerate that already owns 40% of Cathay and is buying 2% more, are Hong Kong-listed companies. But the Chinese government controls both Citic Pacific (through its parent, Citic) and Air China. The details are confusing, but the thrust is simple: Air China and Cathay will deepen their partnership, while Citic Pacific will end a relationship with Cathay that once served as an economic and symbolic bridge between Beijing and the West.

Both airlines stand to gain. Cathay has received an implicit endorsement from Beijing that it will have a future in a country where firms controlled by foreigners can never be entirely confident of their footing. Air China, meanwhile, will gain expertise from an industry leader. It now owns as much of Cathay as it can without being obliged to make a general offer; many believe it aims in the long term to buy the airline outright.

Nothing will happen quickly. Even if Swire Pacific, an old British colonial *hong* or trading company, wanted to sell out entirely—and it emphatically states the opposite—it would take considerable time. Cathay's international route structure is the result of bilateral negotiations between Hong Kong and other countries, and these would all come under review after a foreign takeover. Equally important, any upheaval at Cathay might alienate one of the world's most loyal groups of customers.

Citic Pacific's sale of almost all its stake in Cathay is a sign of how China's relationship with the rest of the world is changing. It was one of China's first "window" companies, through which the government in Beijing took small, indirect stakes in carefully selected Western firms. Before Hong Kong's handover to China, Citic made a big investment in Cathay, which was seen as a clear affirmation by both China and a prominent British-owned firm of the territory's rosy economic future.

But this arrangement has been superseded. Cathay now has direct ties with Air China (in which it holds an 18% stake) and with the authorities in Beijing. The superficial trigger for the realignment of shareholdings was Citic Pacific's need to raise funds in the aftermath of huge losses last year on foreign-currency deals. These resulted in a scandal, and an ongoing investigation, over whether the losses had been properly disclosed. But Citic Pacific's travails, however severe, would have been handled very differently if China felt it still needed a buffer to interact with the West. Instead, this week's deal signals that a new approach has been cleared for take-off.

A row in the champagne industry

Corks at dawn

Aug 20th 2009 | PARIS
From The Economist print edition

A fight about who will bear the cost of the slump in champagne sales

Alamy

AS SALES of champagne bubbled ever higher in recent times, grape growers in the Champagne region enjoyed soaring demand for their produce. They often held some back, feeding speculation and preventing champagne houses such as Veuve Clicquot and Laurent-Perrier from making as much fizz as they wanted to. LVMH, a French luxury-goods conglomerate which owns Veuve Clicquot among other brands, was reduced to courting tiny winegrowers. It even offered help in the fields in order to secure supply.

Now the tables have turned. According to the Comité interprofessionnel du vin de Champagne (CIVC), a trade body, champagne-makers' sales fell by 23% in the five months to May relative to 2008. Stocks are building: there are 1.2 billion bottles of champagne in the region's cellars, according to Bernard Beaulieu, a local mayor and grower, enough to satisfy global demand for four years.

The glut has prompted a battle over this year's harvest. Each year the CIVC determines how many grapes the champagne houses must buy from the growers. In 2008 it opted for a high level of 14,000kg for every hectare farmed. This year the champagne houses, looking for a way to reduce stocks, are pushing for just 7,500kg a hectare. Such a low figure, coupled with lower prices, would mean a big drop in income for the growers, who want at least 10,000kg a hectare. A decision is due by September 2nd.

Growers claim the big champagne houses have deliberately chosen to stock up amid the recession to alter the balance of power in Champagne for years to come. Why did the CIVC set yields so high in 2008, they ask, when a drop in demand was looming? The champagne houses say they did not see the crisis coming. But they are due to renew a large number of contracts covering four to five years with individual growers, and the glut puts them in a powerful negotiating position, says Philippe Feneuil, a grower.

Most feared is LVMH, which has just over 18% of the global champagne market. It may seize the chance to add to its holdings of vines if growers go bankrupt, or it could buy up struggling small champagne houses. Late last year it snapped up Montaudon, a family house founded in 1891. "LVMH behaves in a paternalistic and charming way in Champagne," says Mr Beaulieu, "but behind that they want to take over our business."

Face value

Bank to square one

Aug 20th 2009
From The Economist print edition

Ken Moelis believes that small is beautiful when it comes to investment banking

Bloomberg

THE first investment bank where Ken Moelis worked—Drexel, Burnham, Lambert—failed spectacularly. Another former employer, Donaldson, Lufkin & Jenrette (DLJ), was bought by a bigger rival. The most recent, UBS, is now on government life-support. During his 25-year career in investment banking, in short, Mr Moelis has seen it all. Over that period investment banks have evolved from staid partnerships into huge, publicly traded conglomerates before stumbling, and in some cases collapsing, last year. But Mr Moelis has survived the upheaval, and come up with some ideas about how investment banking could be improved along the way. He is now trying to put them into practice at the bank he founded in 2007, Moelis & Company.

Mr Moelis started out in the Beverly Hills office of Drexel, where he worked with Michael Milken, the "junk-bond king" who was later jailed for fraud. They raised money for cable-television channels and mega-casinos in Las Vegas—both innovative new businesses at the time—with fabled entrepreneurs such as Ted Turner and Steve Wynn. Mr Milken's belief that a small bank with great ideas could shake the establishment made an impression on the young Mr Moelis, despite Drexel's subsequent collapse. Over the course of his career, he says, he concluded that banking conglomerates were too unwieldy to look after clients or employees properly—one reason why he left DLJ in 2000 when it merged with Credit Suisse. Nonetheless, a few months later Mr Moelis agreed to join UBS, another big Swiss bank, to build up its American investment-banking unit. And build he did. It quickly became a leader in almost every branch of the business, from mergers and acquisitions (M&A) to share offerings.

That was not enough for Mr Moelis, who says he still felt uncomfortable at such a big bank. In early 2007, despite the worsening economic outlook, he left to set up a bank of his own. A day after opening Moelis & Company he won the job of advising Hilton Hotels on a $26 billion takeover bid from Blackstone Group—one of the biggest deals of the buy-out boom. As the recession took hold, demand grew for the impartial advice that "boutique" banks offered but that the giants, with their myriad customers and huge proprietary-trading operations, struggle to provide.

Indeed, big banks' share of the world's M&A business so far this year is five percentage points lower than it was last year. Boutique banks, by contrast, have won their highest share ever, at 15%. Both long-established small outfits such as Rothschild and Lazard, and newer ones such as Evercore Partners, have

seen their business expand. But Moelis & Company made the biggest splash, briefly becoming one of the top ten banks in the M&A business in America. Mr Moelis's firm helped Anheuser-Busch, an American brewer, sell itself for $52 billion to Inbev of Belgium, and helped Yahoo!, an internet portal, see off a takeover bid from Microsoft, a software giant.

In the immediate aftermath of the crisis, the big banks resembled patients coming down from ether to Mr Moelis: "Everyone awoke to find that profits generated from leverage and casino-like bets made with the bank's own capital were just illusions." Small banks were able to win lucrative advisory mandates and hire talented bankers from their dazed rivals. Mr Moelis picked up some big names, including Mark Aedy, a former star at Merrill Lynch. In less than two years he has expanded from ten employees in New York and Los Angeles to 230 in six different cities.

Although the sudden seizure of the credit markets and the subsequent swoon of the economy afflicted the titans of the industry most severely, it is now beginning to affect boutiques too, as mergers dry up. But Mr Moelis has already experienced such a drought, during the recession of the early 1990s, when he was head of investment banking at DLJ. At the time, rather than wait for M&A deals to return, he decided to build expertise in loan restructuring, to win business advising the many firms that were struggling with their debts. DLJ's restructuring group became the market leader and Mr Moelis learned that "When you help a client in trouble, you have a client for life." So he has repeated the trick at Moelis & Company as the economy has soured: restructuring now makes up half its business.

Mr Moelis knows he will have to remain nimble while expanding his firm's offerings. This week Moelis & Company announced the opening of an Australian office that will focus on Asian deals. Plans are also under way to underwrite securities and develop a trading platform. He hopes the latter move will address a shortcoming of many boutiques: their inability to access capital markets. Mr Moelis has also hired risk-advisory experts to help clients comb through the arcane financial instruments (probably toxic) sitting on their books. But he is quick to point out that he will not do any proprietary trading or expand into other fields that could lead to conflicts of interest.

Battle with the bulge

Mr Moelis concedes that his firm is unlikely to keep growing so quickly. Just as the crisis provided an opportunity, the recovery is posing a threat as big banks recapitalise and prepare to wrest business back from the boutiques. Worse, talented bankers from fallen giants such as Lehman Brothers and Bear Stearns are now setting up their own boutiques, further stiffening the competition. Moelis & Company fell to 82nd in the most recent M&A league tables. That decline, although offset in part by restructuring work, shows how transient success in investment banking can be.

Mr Moelis has proved adept at surviving crises, but the banks he has worked for have not all been so fortunate. Can he build a bank that will outlast him? He is convinced that new ideas and agile management will allow Moelis & Company to flourish. But his own career shows just how easily banks can come and go, in large part because bankers do too.

BT's pension problem

Friends, family and grandads too

Aug 20th 2009
From The Economist print edition

A former industry champion battles decline and a huge pension burden

Illustration by Derek Bacon

AT THE head office of BT (formerly British Telecom) in London it is hard to find any lingering evidence of imperial hubris. The firm that vied for the telecoms industry's top spot in the mid-1990s, promising to be "one of the first great companies of the 21st century", now ranks 28th in its industry by market value. It has long since been overtaken by emerging-market upstarts, including Bharti Airtel, an Indian firm it invested in during its infancy, and by European rivals that did a better job of weathering the dotcom crash of 2000-01. Forget fancy maps charting world domination, or ambitious mission statements—a visitor today to BT's lobby is greeted by the modest hum of the staff canteen.

Yet it is also hard to detect any sense of crisis. And crisis, not comfortable mediocrity, is arguably what BT faces today. After a series of profit warnings and accounting problems, this spring its share price fell below its level when the firm was privatised back in 1984, although it has since staged a partial recovery. BT's creditors now hold paper that is rated just above junk. Worst of all, the balance-sheet has a whiff of Detroit's carmakers: a shrunken business supporting gigantic welfare obligations.

BT has a world-class pension problem. Its scheme has 340,000 members and is, on many measures, badly underfunded. Its trustees say that in the worst case, were BT to fail, part of the scheme's £40 billion ($66 billion) or so of gross liabilities would be covered by a state guarantee. That claim, based on the law that privatised BT, has not been tested in court. And in the medium term the worst case, though unlikely, is no longer unthinkable. What went wrong, and what can be done about it?

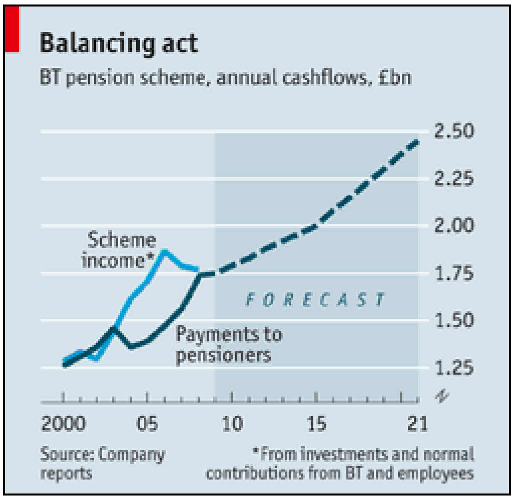
Global problems

The origins of BT's present crisis lie in its previous crisis in 2002, after the dotcom crash. Saddled with debt, the firm sold most of its international assets and span off its mobile operation. That left it looking a lot like the original firm that was privatised: a fixed-line telecoms operator under pressure from both competitors and regulators. Like their predecessors in the 1980s, BT's managers decided to diversify. The incoming boss, Ben Verwaayen, championed BT's Ignite division, subsequently renamed Global Services, which serves governments and big companies. It built a vast order-book of long-term contracts. In the financial year to March 2008 its sales reached £8 billion, almost rivalling BT's traditional business. Judged by awards and customer wins it was a success.

By the test of profits, however, it was not. Even back in 2002, one former executive says, Global's margins were suspect, with heavy capital-expenditure and upfront costs that would, it was hoped, be offset towards the end of contracts' lifespan. In 2007/08 Global contributed almost 40% of sales but just 4% of operating profits. By January 2009, seven months after Mr Verwaayen's departure (he is now the boss of Alcatel-Lucent, a telecoms-equipment firm), BT said even those meagre profits had been seriously overstated. Since 2006 it had capitalised more and more costs, keeping them out of its income statement. Including these and capital expenditure, Global lost at least £800m last financial year. Since 2000, including acquisitions, it has burned up almost £5 billion, equivalent to half of BT's current market value.

Far from being the main source of growth for BT, Global has become a big drain on it. Last year BT's free cashflow before dividends slipped to £737m, 40% of the level of the year before and a third of the level a decade ago. This year BT is expected to generate about £1.3 billion. That has to support dividend payments to long-suffering shareholders, now cut down to about £500m a year, and underwrite the giant and underfunded pension scheme.

Measuring the hole has always been controversial. Since 2000, when new accounting rules came into force, BT has argued that because its scheme invests in risky assets, such as shares, it is likely to outperform government bonds, closing the funding gap. Since then an entire stockmarket cycle has taken place and the position, although volatile, is worse than ever. Using accounting rules, the deficit was £8 billion in June. Taking a tougher methodology and discounting the liability at government-bond rates, the deficit was about £20 billion, or 1.4% of British GDP. An alternative approach is to look at the money the scheme pays out to pensioners, compared with the money it gets from investment income and contributions from BT. Last year the books only just balanced. Payments to pensioners will continue to rise (see chart), before dropping off after 2035.



With luck, the scheme's investments will keep pace. If they do not BT will probably have to make "top up" payments. Since 2000 it has made £3 billion of these, and under a new agreement with the pension regulator it will inject another £1.6 billion over the next three years. That seems inadequate: at that pace it would take between 15 and 38 years to plug the current hole, during which time BT's fixed-line operation could well shrink further. Unless investment returns are strong, the pensions regulator may have to get tougher, forcing BT to direct more and more of its cashflow towards plugging the gap. The danger, in short, is that over time BT will become a firm run for its pensioners.

Cost-cutter Livingston, I presume

That is a fate which Ian Livingston, BT's current boss, a cheery Scot who has been at the firm since 2002, laughs off. His task is to create breathing space by pushing cashflow above the £1.3-billion mark. For a start, there is Global, where he wants to see "conservative accounting and aggressive delivery". Most analysts expect losses to drop to several hundred million pounds this year and it is, he says, "a business that can produce cash". Yet Global has lost money every year since its inception in 2000. It would be hard to shut because a big chunk of its customers and capital expenditure are in Britain, making it tricky to disentangle. The best that shareholders may be able to hope for is that the losses will be plugged, and that eventually BT might be able to sell part of Global to a bigger operator such as America's AT&T. A full takeover of BT is inconceivable given its pension-fund liabilities.

Better opportunities to boost cashflow may come from cutting costs. In fixed-line telecoms that means cutting labour, which comprises about half of BT's expenses. Some 15,000 jobs went last year and a similar amount may go this year, reducing BT's employee base to 100,000 direct staff and 32,000 contractors. That rivals the efforts of KPN, a Dutch rival famous for running a tight ship. Yet for BT, the expected decline in sales this year of 4-5% will eat up much of the £1 billion-plus it plans in savings. Sales will probably carry on falling, as BT's traditional voice products are eaten into by new technologies and competition. Although BT has some new products, such as internet TV, these are unlikely to make a big contribution to profits, not least because its rivals, including Sky, have similar strategies. Recent efforts to branch out into new areas, such as a re-entry into mobile telecoms using network capacity leased from other firms, have not come to much.

In short, to maintain—let alone increase—its cashflow in the

medium term, BT will probably have to cut costs more deeply. That will be hard. About a third of the planned savings are from cuts to capital expenditure, which has reached historically low levels. And the bulk of current job cuts are from a fast-shrinking pool of contract staff, not BT's direct employees who are highly unionised. They have shown restraint on pay (there will be no rise this year) but have historically enjoyed a de facto agreement that there will be no compulsory redundancies. Ripping that up would be an explosive act. One union representative says "we would go toe to toe" with management if compulsory redundancies were attempted.

The last time BT took on the unions was in 1987, when there was a national strike. A senior executive from that era says the confrontation helped demonstrate managers' resolve. Even so, he says, when BT went on to cut about 80,000 jobs in the early 1990s, it had to do so in co-operation with the unions, and pay workers big redundancy packages. In 1994 alone BT paid out almost £1 billion to tempt staff to leave. Today, with cashflow so tight, BT cannot afford to offer such inducements. In any case, Mr Livingston, an avowed cost-cutter, says the "heart attack" approach to job cuts is often counterproductive. He maintains that a steady reorganisation of the business can extract a constant stream of big savings.

BT's pride did not survive its first fall from grace in 2001, but the implicit contract between shareholders, employees and retirees did. They may all have been promised too large a share of a much-reduced pie. For each party to get what it wants, several bets will have to come good over the next five years or so. The equities in the pension scheme will have to outperform government bonds by a decent margin. Global will have to break a decade-long habit of losing money. BT will, for the first time in a generation, have to produce industry-leading new products. And a unionised workforce will have to shrink without employees being offered big financial inducements to leave.

What happens if these bets fail? A confrontation with workers, perhaps, combined with a rapid shift to replace BT's copper network with fibre-optic technology, which by some accounts could free up a fifth of the workforce. That might require BT to raise fresh equity in order to bear the upfront costs. But it seems just as likely that the contract between the company and pensioners—its single biggest problem—will eventually have to be revised.

One course would be to try to cut benefits. Although existing employees have made concessions, such as higher retirement ages, it is near impossible to reduce the payments made to existing pensioners. Detroit's carmakers needed to enter (or flirt with) bankruptcy before their welfare obligations could be watered down. BT is nowhere near that point, and even if it did fail, it says the state would guarantee much of the scheme.

Sharing the burden

The alternative way to socialise the cost of pensions is stealthier. Ofcom, Britain's telecoms regulator, is considering whether to allow BT to include the cost of pensions when calculating the fees it charges rival firms to rent bits of its network. If Ofcom says yes, some of BT's legacy pension costs could be passed on to consumers. The regulator in at least one privatised industry, water, has already made this move. If widely adopted it would be a big step towards pushing the burden of Britain's private pension schemes onto the wider public. Liberalisation would have come full circle: rather than policing companies' returns, regulators would set consumer prices to help their former employees.

BT is furiously trying to revive itself, and has several years to do so. This is no ordinary corporate turnaround attempt, however. The consequences of failure would be severe. There is a slim but real chance that the company, once the standard-bearer for privatisation in Britain and beyond, might eventually have to rely on the helping hand of the state.

America's housing market

Where it all began

Aug 20th 2009 | NEW YORK
From The Economist print edition

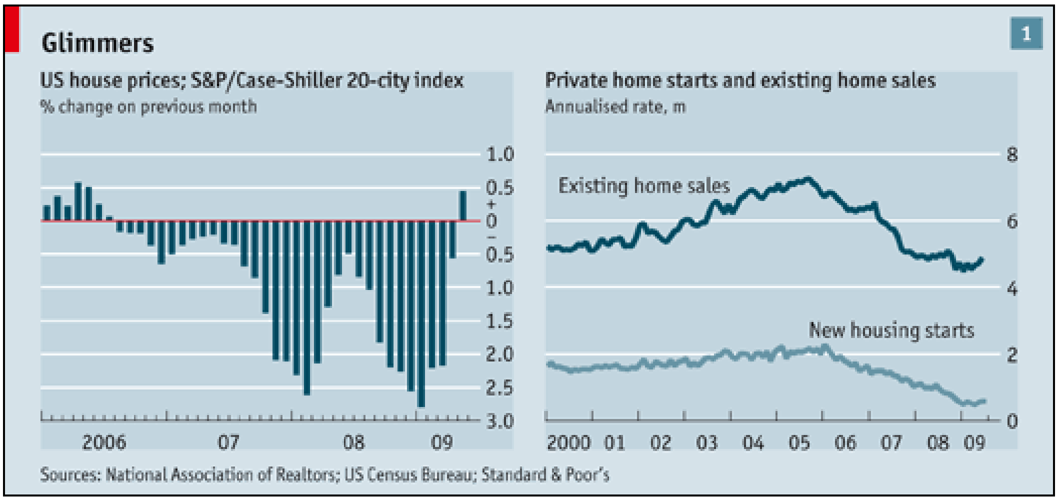
Signs of stabilisation should not obscure the big problems still ahead

Illustration by S. Kambayashi

HE IS hardly your typical distressed seller. Hugh Hefner recently sold his personal residence in Holmby Hills, California, next door to the Playboy mansion, to a 25-year-old entrepreneur for $18m—some 36% below the asking price. It will come as little solace to the ageing Lothario that the discount looked about right: house prices have fallen by one-third from their peak nationwide, and by much more than that in the worst-hit states, such as California, Florida and Nevada.

Although global financial sickness first erupted in American residential property, thanks to ludicrously lax subprime lending, policymakers have recently seemed more worried about asset classes to which the infection subsequently spread. When the Federal Reserve this week extended the life of a facility to support asset-backed securities, for instance, it was more out of concern for commercial property than for housing. Nevertheless, observers agree that America's economy—and all those banks still saddled with underperforming mortgages—will struggle to recover while house prices are still falling. The Obama administration's economic successes "will be for naught" if the housing free-fall continues much longer, says Mark Zandi of Moody's Economy.com.

Hence the excitement over some recent, albeit tentative, signs of stabilisation. The S&P/Case-Shiller index, which tracks home prices in 20 cities, ticked up slightly in May, its first gain in 34 months (see chart 1, left-hand side). New construction of single-family homes rose in July for the fifth straight month. Sales of existing homes are expected to show their fourth consecutive month of gains when latest numbers are released on August 21st (see chart 1, right-hand side). Toll Brothers, a big home-builder, just recorded its first gain in net orders (new orders minus cancellations) for four years. With homes now at their most affordable in living memory, relative to median income, "we've finally found a level where people want to do deals," says Pam Liebman, chief executive of Corcoran, an estate agency. The revival is largely at the lower end, which helps explain this week's $1.4-billion acquisition of Centex, a home-builder which specialises in cheaper houses, by Pulte Homes.



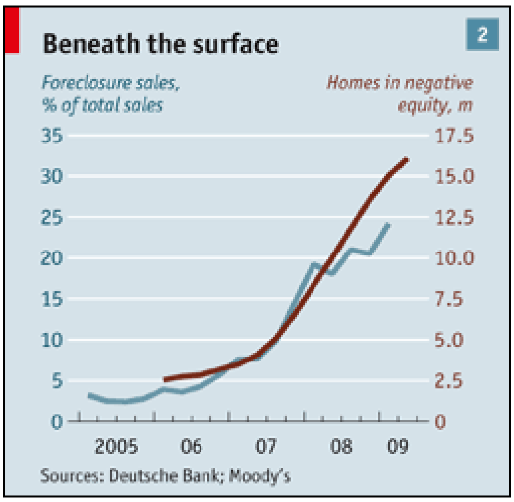
Dig deeper, however, and the recovery's foundations look shaky. Rising joblessness will continue to weigh on demand for homes. The unemployment rate, currently 9.4%, is expected to peak at more than 10% some time next year. The economic effect of unemployment is wider: as more and more of those still in work know someone who has lost their job, they will think twice before buying a property. Consumer confidence remains fragile.

For those seeking a mortgage, credit is still hard to come by. The two main federally backed mortgage agencies, Fannie Mae and Freddie Mac, have tightened their standards for new loans (though mortgages handled by their sibling, Ginnie Mae, have fallen in quality). A Federal Reserve survey of loan officers, released on August 17th, suggested that banks will remain tight-fisted for some time. They are still grappling with growing losses from residential mortgages. These will not peak until early next year, reckons Betsy Graseck of Morgan Stanley.

Moreover, the positive signs in housing are partly driven by short-term factors. One is the tax credit for first-time buyers that was included in Mr Obama's stimulus package: some are rushing to buy now because deals must close by November 30th to qualify. Annual tax refunds, handed out in recent months, may also have given the market a temporary lift. Attractive mortgage rates helped, too. But these have climbed off their historic lows, despite efforts to keep them down through the Fed's purchases of mortgage-backed securities. Many expect them to rise further as ballooning government borrowing puts upward pressure on Treasury yields.

A glut of supply will also weigh on prices, thanks to a wave of repossessions. Foreclosures are running at record levels, with one in 355 of the nation's homes receiving a filing in July alone. Seized properties now account for almost one in four sales (see chart 2). Increasingly, those losing their homes are supposedly safer borrowers with "prime" mortgages. They now account for more foreclosures than subprime borrowers, says the Mortgage Bankers Association (MBA).

With 1.8m homes already in foreclosure, a "similar amount" may be heading that way, reckons Torsten Slok, an economist at Deutsche Bank. Even those states that were the first to feel pain are still seeing a sharp increase in pre-foreclosure notices. In California one type of notice, for "trustee sales", leapt by 32% from June to July, according to ForeclosureRadar, a website. Even more worryingly, delinquencies, the raw material for foreclosures, are still on the rise across much of the once-golden state. In Orange County nearly 7% of mortgages are at least three months overdue but not yet foreclosed, up from around 5% at the start of the year.



The rise in negative equity—when a borrower's mortgage debt exceeds the value of his home—is also fuelling foreclosures, not least because many would rather walk away than keep making payments on a home that is worth much less than the sum owed on it. Zillow.com, a property-information service, estimates that 23% of homes with mortgages are underwater. Others put it higher. A staggering 60% are submerged in Las Vegas. Deutsche Bank's securitisation team expects negative equity to peak at 48% of total homes by 2011. That may be too pessimistic, but all agree that the number will rise further. This matters because negative equity weighs doubly heavily on home prices, by both weakening demand (it traps potential

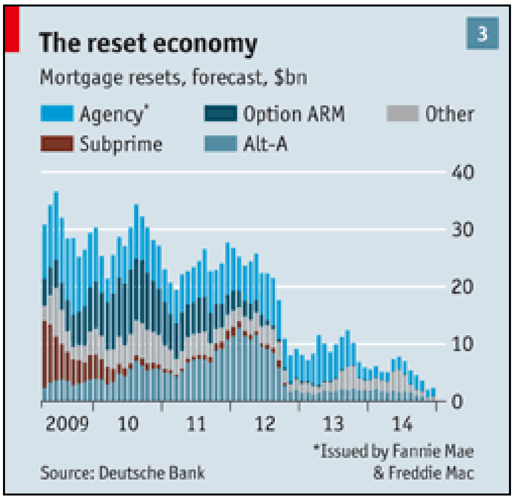
buyers in their homes) and adding to supply (it often ends in seizure and distressed sales).

Government efforts have done little to stop the rot. Under the main foreclosure-prevention programme, only 235,000 struggling borrowers have had their loans altered to make payments more affordable, out of 4m targeted for help. Even with a financial incentive to modify, loan servicers remain reluctant. Many borrowers are too deep in negative equity and the redefault rate is too high. "It doesn't help if you're drowning in 20 feet of water instead of 30," says Jay Brinkmann, the MBA's chief economist. Moreover, the typical troubled mortgage is getting harder to modify because it is more likely to be the result of unemployment than an interest-rate increase. Bringing the monthly payment down by 20% does not help when the borrower has no job.

Even if the pace of modification quickens, the overhang of unsold homes will remain dauntingly large. The inventory represents 9-10 months of supply, three times the level in a tight market, says Stan Humphries, Zillow's chief economist. Paradoxically, a further wave of supply could crash over the market if it is widely seen to be stabilising. Many homeowners who sat tight while prices fell will try to sell at the first sign of a turnaround, according to surveys. In one, conducted by Zillow in July, 29% of respondents were at least "somewhat likely" to put their home on the market once the market perked up. The release of this "shadow inventory" could smother the recovery before it gathers speed.

Just as worrying is the possible recurrence of "payment shock" as interest rates on adjustable-rate mortgages reset higher. Resets on subprime loans have mostly taken place, but the worst is yet to come for some other loans, especially the "Alt-A" category between prime and subprime and a nasty type of mortgage called an "option ARM" (see chart 3). The impact may be muted, but only if the Fed can keep short-term rates very low for the next couple of years—or if the borrowers can refinance as the reset approaches.

Given these downside risks, the recent pop in house prices will probably fizzle. Most economists expect them to fall by a further 5-10 percentage points, to their long-term trend line at roughly 40% below their peak, and not to reach bottom until some time in 2010. The pessimists predict they will go crashing through the trend-line to as little as half their 2006 high.



Analysts at Goldman Sachs, no fools when it comes to housing, hint at several years of stagnation. They argue that the rate of home ownership, currently just over 67%, will fall back to the 64-65.5% level that prevailed before prices took off in the mid-1990s, cutting deeply into demand for properties. This view is supported by a recent Fed study, which found that more than half of the boom-era rise in ownership was due to "innovative" mortgage products, many of which are now history.

It could be even worse. Now that the myth of ever-rising house prices has been shattered, it may be time to embrace another inconvenient truth: that prices can take decades to recover, at least when adjusted for inflation. A study in June by the Federal Housing Finance Agency, a regulator, pointed out that in parts of Texas house prices still languish some 30% below their 1982 peaks in real terms. Mr Hefner may not have got such a bad deal after all.

Housing derivatives

Spark of invention

Aug 20th 2009
From The Economist print edition

A new way for homeowners to hedge themselves against property crashes

Bridgeman

Hothouse of financial innovation

FIRE insurance was not given much thought until the Great Fire of London alerted people to the danger of combining dozy bakers and wooden houses. It took two world wars for life insurance to take root. Some think that the housing meltdown is poised to be a similar catalyst for derivatives that allow investors to hedge against movements in the price of residential property.

Housing derivatives first appeared in 2006 as futures contracts on the Chicago Mercantile Exchange but were only available to sophisticated investors. In the euphoria of the bubble, builders and developers showed little interest in the idea. Smart investors preferred to make bearish bets via more bespoke instruments. But in June, Robert Shiller and Karl Case, two economists responsible for a widely used gauge of American house-price movements, opened up the market to retail investors with the launch of a product called MacroShares.

Derivatives have a bad name at the moment, but this sort is tame enough. MacroShares are securities that reflect the value of the S&P/Case-Shiller home-price index in ten large urban centres. The securities are issued in pairs, one for investors who wish to bet on the upward movement of house prices, and one for those who think prices will fall. That means every bet has an offsetting investment. Investors must also pay for their interest upfront, eliminating counterparty risks. And unlike actual homes, MacroShares are traded on public exchanges and are therefore liquid.

The idea has merit. For most people, their homes are their largest single investment. Finding a way to hedge that investment makes sense. Falling prices are accentuated in illiquid markets such as residential property. Having some protection against price falls should reduce concerns over paper losses.

The next step is to tie derivatives more tightly to the interests of individual homeowners. MacroShares is already mulling a product tied to specific locations, rather than national house-price movements. A homebuyer in Miami, say, could offset the risk of price decline in the local area with a housing derivative. Lenders could end up wrapping these derivatives into mortgage contracts as a form of home-equity insurance. That would be an improvement over some of their recent offerings.

Although trading in MacroShares has been light so far, Mr Shiller thinks the only obstacle to widespread adoption is a deep-rooted belief that home prices always increase. If ever there were a time for that to weaken, it is now.

Monetary policy

Tight corners

Aug 20th 2009
From The Economist print edition

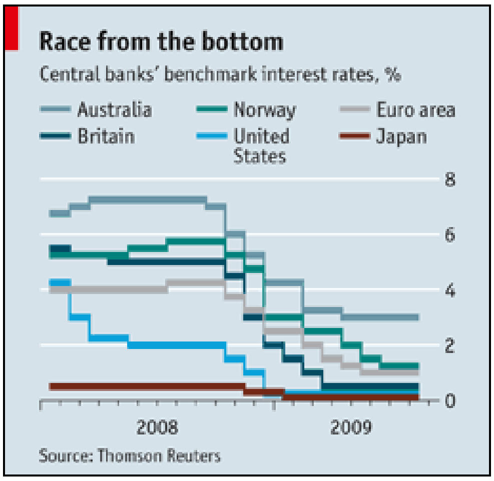
Which central bank will raise interest rates first?

FEW central-bank governors flying into Jackson Hole, Wyoming, for the Federal Reserve Bank of Kansas City's annual economic symposium this week are worrying yet about when to raise interest rates. Having exhausted their usual ammunition, the world's big central banks are still trying to kick-start their economies with unconventional policies. Minutes of this month's rate-setting meeting at the Bank of England, for example, show that Mervyn King, the governor, wanted to expand the bank's asset-purchase plan even more aggressively than it eventually did. But the Reserve Bank of Australia (RBA) and Norges Bank, the Norwegian central bank, are the hawks among the doves. Economic commentators expect them to raise interest rates sooner than anyone else. The near-term yield curve on the pair's government bonds is steeper than in most other countries, suggesting the markets agree.

Which central bank will move first? Australia's economic outlook is brighter than many expected. Although GDP dipped a little at the end of last year, the economy has avoided a recession and the unemployment rate has flatlined at 5.8%, below its long-run average of 7%. Levels of consumer and business confidence are pushing two-year highs, and the RBA's latest statement predicts economic growth for the next two years.

Norway's outlook is rosy, too. Although its economy has shrunk a little, its central bank observes "renewed growth" and its unemployment rate of 3.1% remains the lowest in Europe. Domestic demand has remained strong, and Norwegian employers are reluctant to cut staff when they sense an imminent upturn. Because both countries primarily export staples like raw materials and food, their sales abroad have held up relatively well. Australia in particular benefits from Asian customers whose economies have remained pretty robust.

Big rate cuts were meant to bolster confidence in the face of uncertainty as much as stimulate demand. Even so, some argue the banks overreacted to begin with. Bjorn Wilhelmsen from First Securities, a financial-services firm in Oslo, says most market economists in Norway think the Norges Bank cut rates too much. Both banks have cumulatively slashed their key interest rates by more than the Federal Reserve and the European Central Bank (see chart). In Australia interest rates are at 30-year lows, which seems disproportionate to the amount of economic misery. Rate cuts in Norway and Australia are more potent than those in the euro area and America because floating-rate mortgages are common: more households have more disposable income when interest rates fall.



Deciding precisely when to tighten is tricky, however. In neither country did residential-property prices fall much from their 2007 peaks. And the latest data suggest house prices are increasing again. In Sydney and Melbourne prices rose by about 5% in the three months to the end of June; they rose even faster in Oslo.

That said, the traditional harbinger of rate rises, consumer-price inflation, remains relatively benign. Norges Bank and the RBA are forecasting domestic inflation rates below 2.8% for the next few years. Continued economic hardship overseas also makes central bankers wary of tightening too early. If trends continue, however, Norway's central bank is the more likely to shift its rate first. Its 1.25% benchmark interest rate is below the RBA's 3%; and similar rates of inflation mean the real rate of interest is lower, too.

South Africa's economy

Late starter

Aug 20th 2009 | JOHANNESBURG
From The Economist print edition

Africa's biggest economy is still contracting. But the worst may be over

SOUTH AFRICA was rather slow to feel the impact of the global economic downturn. As other countries start to report their emergence from recession, its recovery is likely to lag behind the rest of the world, too. Output in Africa's biggest economy shrank by an annualised 3% in the second quarter, its third quarterly contraction in a row. This was nevertheless half the 6.4% decline notched up in the first three months of the year, leading many to believe that the worst of South Africa's first recession in 17 years may be over.

For now, however, the pain continues. Almost half a million jobs were lost in the first half of the year, out of a total official workforce of 17m; a further 300,000 are expected to go by the end of the year. Officially, one in every four people in the formal economy is now unemployed. Count those too discouraged to go on looking for a job, and the figure is nearer one in three. There is no sign yet of the 500,000 new jobs that President Jacob Zuma pledged to create before the end of the year.

The employment situation is not helped by unions pressing struggling businesses for double-digit wage increases, backed by a wave of often violent strikes. Local-government workers have already settled for a 13% rise—way above the 6.9% inflation rate—and other public-sector workers are holding out for claims of up to 15%. Less coddled workers in the private sector have tended to be slightly more moderate in their demands, with pharmaceutical workers accepting a 10% wage hike and those in the chemical and paper industries settling for just 9%. But workers at Impala Platinum, a miner, are threatening strike action in pursuit of a 14% rise.

Mining is one of the few areas of South Africa's depressed economy that has already begun to bounce back. Thanks to the rise in global commodity prices, it expanded by 5.5% in the second quarter, after crashing by 33% in the previous quarter. Manufacturing remained in the doldrums. Agriculture and financial services also shrank. But the biggest disappointment was retail and wholesale trade, where the second-quarter decline accelerated to 4.5% from 2.5% in the first quarter.

South Africans remain reluctant to spend, despite the Reserve Bank having slashed interest rates by five percentage points since December. On August 13th the central bank's monetary-policy committee trimmed rates by a further 0.5 percentage points to 7%, a surprise given that it had kept them unchanged in June. While accepting that there were still threats to inflation, notably from big wage hikes and rising oil and electricity prices, it deemed the risk to growth much more important.

Even as it trails others out of recession, South Africa looks less bruised than many. Its sound banking sector (rated 15th out of 134 countries by the World Economic Forum), and the government's commitment to spend 787 billion rand ($98 billion) on infrastructure over the next three years have shielded it from the worst of the global storms. Analysts reckon the economy will shrink by just 1-1.5% this year, before resuming slow growth in 2010.

Carbon markets in China

Verdant?

Aug 20th 2009
From The Economist print edition

The first domestic purchase of carbon credits is less than it seems

AP

Green meets grey

CHINA is the world's largest supplier of carbon credits. The country is due to generate 55% of all certified-emission reduction credits (CERs), which under the Kyoto protocol allow companies in developed nations to offset their emissions by buying credits from developing nations. But to date China has not been a source of demand. So when Tianping Auto Insurance, a Shanghai-based company, bought credits equivalent to 8,026 tons of emissions on the China Beijing Environment Exchange, an emissions-trading platform, earlier this month, analysts sat up. It was the first known example of a Chinese company buying credits to offset emissions.

If Tianping's purchase signals that domestic demand for carbon credits is growing, that should in theory help the fight against climate change. Investment in low-carbon projects, which range from installing cleaner stoves in homes to building wind farms, is what generates credits. The greater the demand for credits, the more attractive such projects become. So is a new Chinese boom, this time in carbon, now on the horizon?

Not quite. What Tianping bagged were voluntary, or verified, emission reductions (VERs). Voluntary credits are an increasingly popular means for companies to burnish their green credentials (although the crisis has muted demand recently). Last year over-the-counter transactions of VERs globally hit a record $397m, according to data from New Energy Finance (NEF), a research firm. Tianping bought credits from last year's Beijing Olympics, supposedly generated by commuters who opted for eco-friendly forms of transport.

Tianping's voluntary purchase shows that the concept of corporate social responsibility is no longer entirely foreign in China. But the idea is still in its infancy. A study by Syntao, a consultancy in Beijing, found that from January to November 2008 just 121 Chinese companies published "sustainability reports". Awareness of carbon offsets remains low. Tianping's $40,000 purchase was small by Western standards. And the credits were first auctioned in December—hardly a sign of feverish demand. Worryingly, they also appear not to have been audited by specialists in line with the highest standards for voluntary credits, says John Romankiewicz at NEF: it is hard to be sure, for example, that people really rode their bikes to work during the Olympics rather than jumping in taxis.

For domestic demand to take off, Chinese firms will probably have to be pushed. Setting a limit on companies' emissions beyond which they must buy offsets is not thought to be on the cards, but hopes are growing that China will commit to some kind of non-binding target, possibly at the Copenhagen climate-change summit at the end of this year. Chinese negotiators recently gave a timetable for a peak in the country's emissions, albeit in far-off 2050. In June, China's state council said it plans to set a "carbon intensity" target, which would determine a certain level of emissions per unit of GDP. But detailed policies may not take shape until the launch of the next five-year plan, beginning in 2011. Tianping's move is still a rather solitary shoot of greenery.

Reforming finance: Resolution regimes

Fail-safe

Aug 20th 2009
From The Economist print edition

The problems of winding up huge financial firms. The latest in our series

THE failure on August 14th of Colonial BancGroup of Alabama, a lender with $25 billion in assets, was also an example of a continuing success story: America's resolution regime for deposit-taking banks. The Federal Deposit Insurance Corporation (FDIC) calmly seized the bank and sold its branches and deposits to BB&T, another bank. Borrowers continued to make their repayments. Contrast that with the slow-motion failure of Britain's Northern Rock early on in the crisis, where Parliament had to pass emergency laws to take the bank into public ownership.

It makes sense to have special insolvency procedures for banks. Traditional court-led resolutions used by ordinary companies proceed too slowly. Banks are subject to losses of confidence that can infect the entire financial system. Taking action only when a bank is insolvent is too late. The FDIC, for example, can step in if a bank's ratio of tangible equity to total assets drops below 2%. America has learned, however, that such considerations do not just apply to banks. When troubles emerged at Bear Stearns, Lehman Brothers and AIG last year, American authorities were hamstrung. Because none was technically a bank, the authorities could not intervene in the way they did with Colonial.

These flaws are being addressed. Bills sent to Congress late last month would allow the Treasury to appoint the FDIC or the Securities and Exchange Commission as receiver for any large "financial holding company" that posed a threat to financial stability, although regulators are squabbling over who would get to make the final decisions. For its part, Britain has had a new bank-resolution regime since February, one that the International Swaps and Derivatives Association considers "state of the art". Now, when the Financial Services Authority, a regulator, judges a bank (or insurer) of any size to be dangerously close to insolvency, the Bank of England can seize control, bring it into public ownership or sell parts of it to other banks.

Winding up the biggest financial firms will still be hideously tricky, however. Private buyers are less likely to be able to swallow them whole, for one thing. Counterparty networks are more complex. In both Britain and America regulators are asking firms to produce "death plans" that lay out how they can be efficiently liquidated or dismembered under financial stress. The American Treasury's experiences with Bear Stearns and AIG showed that these firms would be almost impossible for a government administrator to carve up in a crisis without an instruction manual.

Illustration by S. Kambayashi

Larger firms tend to be international ones, too. Companies like Citigroup or HSBC operate with intricate corporate structures across different jurisdictions, yet it is not clear how they would be resolved across borders. America has long operated a nationalistic insolvency regime that ring-fences the domestic assets of banks that become insolvent, whether they are American or foreign, in order to compensate American deposit-holders. More effort should have gone into clarifying international insolvency, say some. "Britain might introduce a new special resolution regime, but it won't work properly if that institution has branches in America," says Robert Bliss of Wake Forest University.

Larger financial firms also benefit from an implicit government guarantee that they will be bailed out if they get into trouble. In theory, resolution regimes could help instil greater market discipline by specifying ahead of time what would happen to shareholders and creditors in the event of a failure: mandatory haircuts, say, or compulsory debt-to-equity conversions. In practice, official proposals have not yet headed down this path. Having bailed out so much of the system this time round, promises not to do so again ring a touch hollow.

And if they were seen as credible, pre-specified losses would hike the costs of bank financing.

As it is, creditors' rights have arguably been weakened by the new and proposed resolution regimes. Because tottering banks in America and Britain can be seized before they are even insolvent, some reckon that shareholders' property rights are at risk of being illegally infringed. Others worry that creditors of failing financial firms have no judicial recourse. "In ordinary bankruptcy proceedings, the creditors do not get to make the decisions about how to wind up the afflicted firm, so why should the government when it becomes a creditor?" asks Mr Bliss.

Payment cards and the poor

A plastic prop

Aug 20th 2009 | NEW YORK
From The Economist print edition

Schemes to distribute aid and benefits

EARLIER this year more than 1.5m residents of Pakistan's Northwest Frontier Province (NWFP) fled their homes to escape fighting between the army and Islamist militants. Faced with the problem of distributing aid in a region with an honour code that frowns on cash handouts, the government turned in June to a local bank and Visa, a card-payments network. Within a week they began issuing pre-paid debit cards. Some 230,000 cards—one per displaced family—were handed out, each loaded with $300 per month that could be spent on food and medicine at any of 500 terminals in and around their camps.

Using plastic to channel aid and benefits is a growing global trend. Visa is also doing this in the Philippines, Mexico, Brazil, Costa Rica and the Dominican Republic, where 800,000 people get food aid, fuel subsidies and even rewards for attending school on its Solidarity Card. MasterCard, another card network, is active in Poland and Peru. Mature economies have caught on, too: at least 38 American states distribute benefits on cards or plan to do so.

For governments, the savings can be substantial. It costs a penny to put money into an account linked to a card, compared with 60 cents to send out a cheque, says Shane Osborn, the state treasurer of Nebraska, whose card schemes include child benefit and income support. The state has been able to halve its call-centre staff because it now gets fewer inquiries about lost cheques and the like. Card schemes mean less fraud, too. Pakistan's is backed by a database of biometric information.

For recipients the advantages include an end to cheque-cashing fees (of $1.5 billion a year in America alone, Visa claims), convenience (you don't have to be at home to get the money) and greater security (the balance is safe if the card is lost). The card networks and banks, meanwhile, take a slice of every transaction from merchants.

There is also a social benefit. Ali Hakeem, head of Pakistan's National Database and Registration Authority, sees the NWFP scheme as a "massive financial-inclusion programme". The hope is that some of the 95% of recipients who previously had no link to the formal financial system will eventually become regular bank customers because of the scheme, or at least hang on to their cards as a way to save as well as spend.

Economics focus

The unkindest cuts

Aug 20th 2009
From The Economist print edition

Discounting that promotes competition is hard to distinguish from predatory pricing

Illustration by Jac Depczyk

TWO decades before he won the Nobel prize for economics in 1991, Ronald Coase wrote an essay decrying the poor state of research in industrial organisation, the discipline in which he established his reputation. The field, he complained, was devoted to the study of monopoly and antitrust policy. That, he said, made for bad scholarship: an economist faced with a business practice that he cannot fathom, according to Mr Coase, "looks for a monopoly explanation".

A lot has changed in the 37 years since that lament. The broader research effort for which Mr Coase called has fostered a richer understanding of how firms respond to customers and rivals. Monopoly explanations now compete with theories that see the same behaviour as helpful to consumers. That has made it harder to sort malign from benign business practices. The recent antitrust finding against Intel, a maker of computer chips, is a case in point. After a long investigation, ending in a bulky 524-page verdict, the European Union in May fined Intel €1.06 billion ($1.44 billion) for illegally using its muscle to price AMD, a rival chipmaker, out of the market. Intel rejects the charge of predatory pricing and plans a court appeal. Its lawyers have a block of theory on which to build a defence.

Allegations of predatory pricing have a long history. The Sherman Antitrust Act of 1890, the foundation of America's competition policy, was partly a response to complaints by small firms that larger rivals wanted to drive them out of business. Trustbusters need to be wary of such claims. Low prices are one of the fruits of competition: penalising business giants for price cuts would be perverse. But in rare circumstances, a big firm with cash in reserve may cut prices below costs in order to starve smaller rivals of revenue. The profits sacrificed in the short term can be recouped by higher prices once competitors are out of the way.

Establishing that a firm is guilty of predation is difficult. If rivals stumble or fail, that may be down to their own inefficiency or poor products, and not because they were preyed upon. Proving that a firm is pricing below its costs is tricky in practice. Even where a reliable price-cost or profit-sacrifice test is feasible, failing it need not imply sinister intent. There are often pro-competitive reasons to forgo short-term profits. Firms with a new product, or a new version of an existing one, may wish to pick a lossmaking price to defray the cost to consumers of switching, or because they expect their own costs to fall as they perfect the production process (video-game consoles are a classic example). Losses would then be a licit investment in future profits.

Predation is even trickier to uncover when goods are sold together. A firm that enjoys fat profits on one good may "bundle" it with another on which margins are lower. If the discount on the bundle is hefty enough, other firms may struggle to offer as enticing a deal. In 2001 the EU blocked a proposed tie-up between GE and Honeywell for fear that the merged firm might use bundled discounts to squeeze rival suppliers. In 2007 a committee of antitrust experts appointed by the American government proposed a test for whether bundling is predatory. First, assume the discount applies solely to the low-margin good. So if each good sells for $10 separately and $16 as a bundle, allocate the $4 discount to the more "competitive" product. Next, apply a price-cost test: if the product costs over $6 to make, the bundle is predatory.

That check seems neat but sound business practices may still fall foul of it. It may be cheaper for a firm to sell the two goods together, because of cost savings on distribution. Firms also often use bundling as a way of charging high-demand users more. Thin margins on sales of printers, for example, can be made up by bundling in more profitable toners. This kind of "metering" is an efficient way of recovering fixed costs such as research.

Another ambiguous tactic is to offer rebates to customers that reach certain sales targets. Bulk buyers generally pay lower unit prices to reflect suppliers' economies of scale. Rebates can also help align incentives. Suppliers want retailers to promote their products, offer in-store information and keep plentiful stocks. The trouble is, retailers bear all the costs of such sales efforts but reap only some of the benefits. Rebates provide incentives for retailers to drive sales, as profits are bigger once the target is met.

The price of loyalty

The EU reckons that Intel's use of such rebates was nefarious. It is in the nature of rebates that, just above the target threshold, the price of each additional purchase can be negative. If, say, a firm charges $1 for each sale of up to nine units, and a unit price of 80 cents (a rebate of 20%) for sales of ten items or more, the price of the tenth sale is minus $1, since nine units cost $9 and ten units costs only $8. A dominant firm like Intel can rely on a certain market share (an "assured base", in the jargon). It could in theory set a rebate threshold above that mark, where smaller rivals may hope to mount an effective challenge but cannot match the negative marginal prices on offer to buyers.

Intel's conduct was certainly worth investigating. Its rebates kicked in if customers gave the firm between 80% and 100% of their business. The schemes looked like a response to a competitive threat from AMD. Yet the EU's trustbusters cannot feel too sure of themselves. Intel's rival is still alive and kicking: AMD has not been excluded from the market (though its investment plans may have been thwarted and potential entrants deterred). Moreover, such a complex case, with a bulky ruling which is still not in the public domain, does not offer much guidance on what sort of rebate schemes might be deemed predatory.

Trustbusters have moved away from the practice that so concerned Mr Coase in the early 1970s—of being too quick to condemn big firms on the basis of crude judgments. But they are unlikely to find a robust and simple rule to put in place of the old presumption that firms with market power are always suspect.

Better vaccinations

Hypodermic needless

Aug 20th 2009
From The Economist print edition

How to improve the delivery of vaccines

AFP

VACCINATIONS are a pain. Any two-year-old with access to reasonable health care will tell you that. But injections are bad for reasons other than the discomfort they cause. If syringes are reused without sterilisation, they can spread disease. The liquid vaccines they require are often temperamental, needing constant refrigeration and thus what is known as a "cold chain" to keep them in tip-top condition as they move from factory to clinic. And hypodermic needles do not even deliver vaccines to the best place in the body.

Vaccines work by activating the immune system. For that to happen, they have to meet up with what are known as antigen-presenting cells. These cells recognise alien invaders, chop them up and then carry characteristic bits of them to the rest of the immune system so that the invader can be recognised and appropriate measures taken. If an invader is new, this process allows the immune system to learn to recognise it, and respond more rapidly next time. A vaccine (which contains either a dead or an attenuated form of a pathogen) lets the immune system learn about a disease without the body having to undergo the infection. But antigen-presenting cells tend to congregate in places where pathogens arrive, such as the lungs and the skin—not in the muscles where the tip of a hypodermic needle ends up.

How to improve this state of affairs was the topic of two talks at this year's meeting of the American Chemical Society, in Washington, DC. Both proposals eliminate the need for painful needles and the need to transport liquids around. And both deliver their cargoes to places where antigen-presenting cells abound.

Just breathe deeply

Robert Sievers of the University of Colorado is working on a new way to deliver a vaccine for measles. Vaccination against this disease has become controversial in effete Western circles because of the malign effects of one or two hysterically reported scientific studies which suggested (wrongly, it is now believed) that the vaccine might occasionally be hazardous. In many parts of the world, however, measles itself is a serious hazard. It kills about 200,000 children a year, and vaccination—using a liquid vaccine and a hypodermic—is the only way to prevent it.

Because measles attacks through the respiratory tract, though, Dr Sievers reckons this is a better place to send the vaccine than the muscles of the arm. And one way to do so would be to have the person being vaccinated inhale a finely powdered vaccine that coated every inch of his lungs. To make such a powder, Dr Sievers has perfected a trick that atomises liquid vaccine into tiny droplets. When the water evaporates, the particles of vaccine which remain are so small that they can spread through the lungs without clumping.

This is not as easy as it sounds. Atomisation nozzles are commonplace. They are used in everything from perfume bottles to car engines. But a nozzle alone is not enough. The droplets it produces—and hence the granules of the powder—are too big for Dr Sievers's purposes. Instead, he has turbocharged the process by mixing the vaccine with ultra-high-pressure carbon dioxide.

When this mixture emerges from the nozzle, it bubbles like champagne. The bubbles fragment, forming ultra-tiny drops, and when these dry they leave a powder with granules that are between one and five microns across. This powder can be doled out easily in individual doses and inhaled from a bladder—and a monkey that did so was protected from influenza. Human trials are expected to begin next year in India.

Skin fix

Mark Prausnitz of the Georgia Institute of Technology and his team have devised a different way to replace the hypodermic needle. They have successfully inoculated mice against flu using scores of tiny needles that might be referred to as "hyperdermic", because they do not fully penetrate the skin. This method, too, eliminates the need to transport liquid vaccine around.

Dr Prausnitz's vaccine-delivery device is a steel patch with an array of needles, each about half a millimetre long, on it. The array is coated with liquid vaccine mixed with a thickening agent. This dries, leaving the needles impregnated with solid vaccine. The resulting device is robust and reasonably insensitive to heat.

To use it, you press it against someone's skin (possibly your own). The needles painlessly puncture the skin, but do not go through it. Moisture from the body then dissolves the vaccine and it spreads into the skin in minutes.

That the patches are self-applicable is a huge bonus. Dr Prausnitz hopes it might be feasible to send vaccines to people by post during an epidemic, obviating the need for them to go to a clinic.

At the moment Dr Prausnitz's technique, like Dr Sievers's, has been tried only on animals, but it has such elegance and simplicity that if human trials are successful it could prove to be important in controlling influenza. Exactly who should receive influenza vaccine is the subject of this article.

Influenza vaccination

How to stop an outbreak

Aug 20th 2009
From The Economist print edition

A mathematical model suggests a new way to allocate vaccines

THE existing formula is simple. When vaccinating against influenza, inoculate those most susceptible to the disease's wrath. Such vulnerable types include the elderly (who are the most likely to die if infected) and infants (whose immune systems are not fully developed). This seems a reasonable policy, and it is the one that has long been promulgated by America's Centres for Disease Control (CDC). Only recently has it been extended to include children up to the age of 18, on the basis that they are more likely than other people to catch flu in the first place, through enforced socialising at school—even though they are at little risk of dying from it.

According to Jan Medlock of Clemson University in South Carolina, and Alison Galvani of Yale, however, vaccinating those most at risk of bad effects is not the right way to deal with the disease. In a report published this week in *Science*, they argue that even with the extension of vaccination to school-age children, the existing policy of protecting the individual is still playing down the real public-health value of vaccines—namely that they create a so-called herd immunity which helps to break the disease's chain of transmission.

They argue that it would be better to concentrate on vaccinating those most likely to spread the virus—both schoolchildren and people between the ages of 30 and 40, who are likely to be the parents of those children, and who are, at the moment, at the bottom of the vaccination priority list. That, at least, is the outcome of their mathematical model of how influenza spreads. Indeed, it is almost all of the outcomes. For in order to obtain a robust result, Drs Medlock and Galvani considered two different sorts of epidemic and five different definitions of an optimal conclusion.

As model epidemics they chose those of 1918 (the famous "Spanish" flu that is reckoned to have killed 50m-100m) and 1957 (less lethal, but still pretty nasty). As definitions of a good outcome they started with two simple measures: the number of infections averted, and the number of deaths averted. They then went on to look at more sophisticated measures: the number of years of life saved (taking into account the ages of those who would otherwise have died), the "contingent valuation" of those lives and the economic cost of vaccinating.

Contingent valuation is based on surveys of the "disutility" of death at different ages. This provides a crude way to balance what has already been invested in a life against what might come of it. Measuring economic costs weighs the expense of both vaccination and illness against the net present value of the future earnings of someone who would otherwise die from the disease.

Yet no matter which outcome was looked at, nor which pattern of epidemic was chosen, the result was the same. The best approach to influenza is to vaccinate young people and their parents, not infants and the elderly. Moreover, it is a cheaper and more efficient option. Around 85m doses of vaccine are distributed in the United States in normal years. Dr Medlock and Dr Galvani reckon that if their approach were followed, that might be cut to just over 60m.

As luck would have it, though, the new advice agrees more closely with the recommendations of the CDC's advisory committee on immunisation practices about the best approach to the epidemic of N1H1 swine flu that is now circulating. For reasons still unknown, elderly people are not as susceptible to this strain as they are to others, and what deaths there have been have tended to occur among the young—particularly young adults. The strategy of "vaccinate those at risk" thus coincides with "vaccinate the spreaders". A fortunate coincidence, perhaps.

The smell of death

The dogs have had their day

Aug 20th 2009
From The Economist print edition

Analysing the smell of corpses may help to find the dead—and the living

Alamy

IT IS morbid, but true, that one of the ways survivors of natural disasters are found is by bringing out bloodhounds that have been trained to find the dead. Often, when these dogs reveal corpses under rubble, rescuers also find previously undetected air pockets with living people in them. Dogs are useful when police officers are looking for the buried corpses of murder victims, too. Such animals, however, require feeding and housing when they are not being used, and expert handling when they are. It might be better, therefore, if they could be replaced by machines—and that is what Sarah Jones and Dan Sykes of Pennsylvania State University propose to do. As they outlined to this week's meeting of the American Chemical Society, in Washington, DC, they have been analysing the smell of corpses, with a view to automating the process of detecting them.

The idea of doing this is not entirely new, but when Ms Jones and Dr Sykes looked at the previous studies they found that the corpses used were usually at least three days old. That is an almost inevitable delay if human cadavers are employed, since permission must be sought and forms filled in. But the two researchers wanted to know which chemicals emanate from freshly dead bodies, as well as from those that have been around for a few days. So they decided to compromise and work on pigs instead of people. Pigs are often used as substitutes for humans in early-stage medical experiments, as they are about the same size. For that reason, too, they decay at the same rate and go through the same phases of decomposition.

To carry out their experiment Ms Jones and Dr Sykes put dead pigs inside small wooden chambers that were covered with clear plastic sheets. The chambers, which were placed in the middle of a field, prevented large scavengers from coming along and dragging the corpses away. Insects and bacteria from the air above and the grass below, however, had easy access to the bodies.

The chemicals of decay were sampled by three collectors inserted through holes in the plastic sheet. The collectors contained fibres of different compositions, each of which absorbed a unique range of volatile molecules such as organic acids, alcohols, amines and ketones. The fibres were replaced at regular intervals over the course of seven days and taken away for analysis by a device called a gas chromatograph-mass spectrometer.

As Ms Jones and Dr Sykes told the meeting, the composition of the chemicals released by the corpses did, indeed, change over time. Acids made up 32% of the compounds detected in the first two days, but dropped to 25% after the third day. Some of the individual acids that were released, such as pentanoic and benzoic acid, were present throughout all seven days that the experiment was conducted. Some, including tetradecanoic acid, were found early but not late in the decomposition process, while others, such as acetic and propanoic acid, were found late but not early. Similar results were found with other sorts of volatile compounds.

This information will be useful for establishing "time of death" in murder investigations. It could also be used to fine-tune an electronic nose, if such a device were to be used at the site of a disaster. Electronic noses rely on detecting changes in the electrical conductivity of various substances when they absorb particular target molecules, and could easily be brought in to replace dogs if they were thought reliable enough.

For that to happen, more research will be needed. The pigs will have to be staked out in a wide variety of environments, and more experiments on human corpses would be desirable, as well. The result, though, could be lives saved and murderers caught—as well as a few redundant bloodhounds.

Reading bar codes with mobile phones

Snap it, click it, use it

Aug 20th 2009 | SEATTLE
From The Economist print edition

A new way to deliver information to mobile phones is spreading around the world

Alamy

Doing it the old-fashioned way

NEGOTIATING his way across a crowded concourse at a busy railway station, a traveller removes his phone from his pocket and, using its camera, photographs a bar code printed on a poster. He then looks at the phone to read details of the train timetable displayed there. In Japan, such conveniences are commonplace, and almost all handsets come with the bar code-reading software already loaded. In America and Europe, though, they are only just being introduced.

Actually, calling them bar codes is a bit old-fashioned, because they store information in a two-dimensional (2-D) matrix of tiny squares, dots or other geometric patterns, rather than a stripe of black-and-white lines of varying thickness. When an image of the matrix is captured, software in the phone converts it into a web address, a piece of text or a number. If a number, it is sent to a remote computer which responds with an instruction that tells the phone to perform an action associated with that particular bar code.

In the case of the traveller, this might be calling up a web page on which the train timetable is displayed. Other 2-D bar codes might add an event to a calendar or display a coupon that entitles the bearer to a discount on a hamburger. Indeed, one magazine recently featured a bar code alongside archive images of famous swimsuit models. Lecherous readers who photographed it were rewarded with additional pictures.

In Japan, 2-D bar codes appear not only on posters and in magazines but also T-shirts, scarves and even as art. They can even be displayed on monitor screens, allowing people to store a web address for whatever they are looking at on a computer on their phones, for future recall.

In America and Europe, three types of bar code, called QR Code, Data Matrix and Ezcode, are likely to become common. The first two are free, open standards. Ezcode is owned by a New York-based firm called Scanbuy, but it, too, is available free, for general purposes. The firm behind it makes its money by charging advertisers and publishers when people use it.

In July three mobile-phone operators in Spain—Orange, Telefónica and Vodafone—agreed to load software that recognises Ezcode. Scanbuy has also signed a deal with two Danish operators and two in South America. In the United States, a Samsung mobile phone, the Exclaim, has become the first to be sold with Scanbuy's program already loaded.

Meanwhile a Swiss software firm called Kaywa has been collaborating with *Welt Kompakt*, a condensed version of *Die Welt*, one of Germany's leading newspapers, to run QR Codes next to articles. It has also developed software for SBB, the Swiss Federal Railway, so that passengers can scan 2-D bar codes on trains and at stations to call up timetables.

A game of tag

A new format for bar codes appeared in January, when Microsoft unveiled Tag, a system that uses colour to increase the density of information that can be stored. A Tag code occupies about one-eighth of the space of a comparable QR Code. It also allows coding elements to be incorporated into designs. One sample code shows a photograph of coloured jelly beans that includes Tag data. Others show company logos, balloons and birds.

Bar codes that do not need specialised software to read them are also being developed. These encode less information than their more sophisticated counterparts but can be used by people who own simpler mobile phones, because the image-recognition process is handled elsewhere. The codes made by JAGTAG, of Princeton, New Jersey, for example, can be photographed using a camera phone and then sent to a messaging service that analyses the code and sends back appropriate information. *Sports Illustrated* used the JAGTAG system when it sent its readers those extra images of swimsuit models, and the system has also been used to advertise Nike, Sony and a restaurant chain called Qdoba.

Bar codes, then, could be on the point of breaking out of their native environment. It has been a long and curious journey from the supermarket checkout.

Correction: Lightyears

Aug 20th 2009
From The Economist print edition

In “As important as Darwin” published on August 15th, we said that no astronomer can look beyond a distance of 13.7 billion lightyears. This was incorrect. The universe has expanded during the 13.7 billion years that light has been zipping across it and, as a consequence, astronomers can see to distances of perhaps as far as 47 billion lightyears.

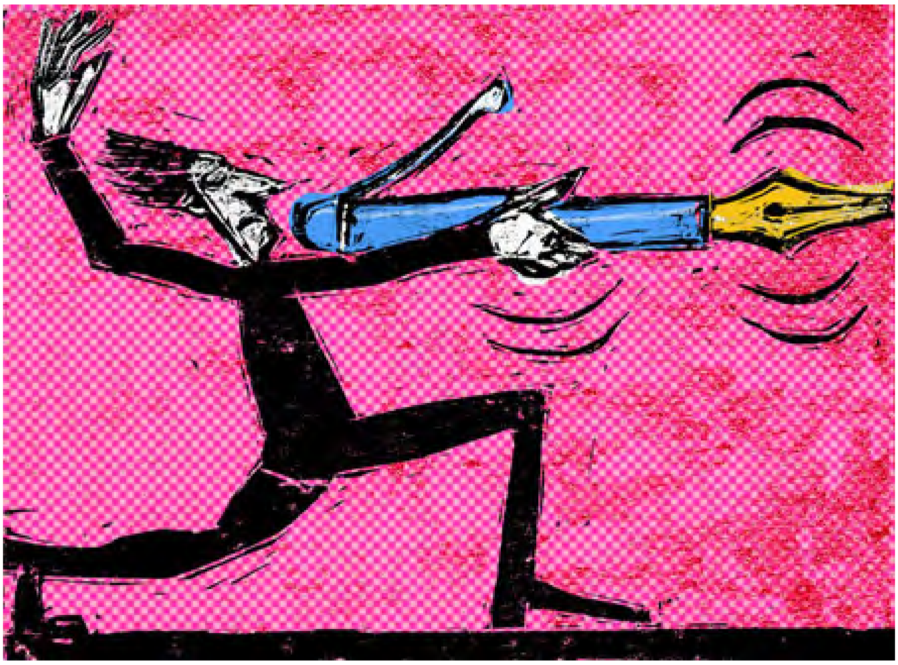
Political philosophy

Mightier than the sword

Aug 20th 2009
From The Economist print edition

The collected thoughts on this, that and the other of two clever men

Illustration by Daniel Pudles



Facts are Subversive: Political Writing from a Decade Without a Name. By Timothy Garton Ash.*Atlantic Books; 441 pages; £25.* Buy from Amazon.com, Amazon.co.uk

Gray's Anatomy: Selected Writings. By John Gray. *Allen Lane; 481 pages; £20.* Buy from Amazon.com, Amazon.co.uk

WHEN writers are grand enough, they can produce books by recycling their journalism, lectures, academic papers and other jottings. Sometimes that can seem dated and lazy. Sometimes it is a treat: the assorted pieces come together to create a great mosaic. Neither "Facts are Subversive" by Timothy Garton Ash, an Oxford-based writer and academic, nor "Gray's Anatomy" by John Gray, a political philosopher, fall into the first trap (or at least very rarely). They are both good reads. But neither quite reaches the goal of the whole being more interesting than the parts.

Mr Garton Ash is incapable of writing a dull article. Unlike some famous-name writers, he is proud to be a reporter: whatever the subject, he digs diligently. He observes sharply and with a dry donnish wit that deserves greater play. A remarkable wordsmith, at his best he has an echo of one of his great heroes, George Orwell. The pieces range from his first stamping-grounds of Germany and central Europe to the bigger themes he took on later (such as Britain's neurotic "don't know, don't trust, don't care" relationship with Europe) and to more exotic places, including Brazil, Iran and Myanmar.

His aim is to chronicle the history of the "nameless decade", the period that began with the terrorist attacks on America in September 2001 and ended with the election of Barack Obama last year. The subjects encompassed in that time include authoritarian governments, the challenge to liberalism raised by Islam and the corrosive combination of the Bush administration's bungled foreign policy and Europe's unthinking anti-Americanism.

But Mr Garton Ash's silver nib wiggles past those constraints. The best essays in the book are timeless. One is a nuanced and convincing piece, both sympathetic and devastating, about Günter Grass, the

German novelist, who revealed in his memoirs that he had briefly been in the *Waffen* SS. Did that taint Mr Grass's books, or his role in public life, or both or neither? Was it the wartime service that was shameful, or its concealment over decades? Mr Garton Ash brings the reader sure-footedly through the thickets of Germany's post-war history and through the marshy ground of moral relativism. He points to the real scandal: that Mr Grass was himself so casually splenetic over so many years about other people's shortcomings, while concealing his own.

Another excellent piece touches on a comparable issue: the list of suspected communist sympathisers that Orwell supplied to the British authorities in 1949. Again, Mr Garton Ash is scrupulously fair, highlighting Orwell's sincere (and justifiable) fear of communist infiltration, as well as his fumbling feelings for Celia Kirwan, the British official involved.

Some of the reworked articles are commendable journalism, but do not quite stand the test of time. Mr Garton Ash's observations from his trip to Iran in 2005 seem a bit whiskery now. It is nostalgic to read about the fall of crony capitalism in Ukraine five years ago. But the reader is left hankering to know what Mr Garton Ash thinks about the mess that has succeeded it. A fiercer editor might have left out such pieces, and pruned the author's occasional lapses into self-indulgence (using "proleptic" once is fine, twice is tiresome). That may not matter in individual newspaper columns. It jars when collected in a book.

Mr Gray's book is darker, grittier and more ambitious. Mr Garton Ash is happy to lambast the West's specific shortcomings but Mr Gray sets out to unpick the shallow philosophical foundations of the whole edifice, in particular the modern myths about progress and perfectibility. He demolishes the theory that we have reached the "end of history", the dogmas of secular liberalism, the weaknesses of financial casino capitalism and the limits of energy-intensive economic growth. Such targets deserve his scrutiny and Mr Gray's criticisms are cogent. But he tends to overdo it. Again and again (and again) he attacks the people he calls "neoliberals" without pinning down whom (apart from Tony Blair) he is attacking. The reader is left feeling a straw man has been dissected.

The finest pieces in Mr Gray's book are satire. One is a Swiftian essay in favour of torture (which some serious-minded lefties took at face value). Even better is a devastating parody of the Marxist approach to linguistics, involving a (fictional) visit by Ludwig Wittgenstein to the Soviet Union, and his relationship with an (invented) Hungarian academic, L. Revai, who idealises the grunts of slave labourers as a proletarian *Ursprache*.

In Mr Gray's most substantial essay, "An agenda for Green conservatism", he attempts to rescue conservatism from the ideological excesses of the 1980s. This is a thought-provoking enterprise, deserving a book on its own. But if it became a book, the author's views on such things as the failings of professional monopolies in education and health would benefit from more statistics and fewer assertions—calling, perhaps, for investment in a researcher. As Mr Garton Ash rightly points out, it is facts, ultimately, that are subversive.

American conservatism

Overdoing it

Aug 20th 2009
From The Economist print edition

The Death of Conservatism. By Sam Tanenhaus. *Random House; 144 pages; $17.* Buy from Amazon.com, Amazon.co.uk

THE recent implosion of the conservative movement is one of the great puzzles of American political history. Four years ago the Republican Party was in charge of the White House and both chambers of Congress. Today the party is locked out of power in Washington entirely, confused about its future and dominated by its know-nothing fringe.

Sam Tanenhaus, the editor of the *New York Times Book Review*, is well qualified to explain this extraordinary debacle. His biography of Whittacker Chambers, a Communist turned conservative hero, was first-rate, and he has been working on a magnum opus on William Buckley, a more recent conservative hero, for years.

Eyevine

Is Bill O'Reilly conservatism's mortician?

Mr Tanenhaus argues that the Republican Party's losses in 2008 were not mere temporary setbacks but the death throes of a political movement. Conservatives may continue to produce a great deal of sound and fury. But they signify nothing. They are locked in the past: obsessed by problems that the rest of the country has gone beyond (such as gay marriage) and incapable of offering solutions to real calamities, such as the recent economic crisis. As policymakers struggled to save the economy from collapse earlier this year, conservative activists railed irrelevantly about "liberal fascism".

Many conservatives blame their recent failures on George Bush's "betrayal" of the conservative movement. Mr Tanenhaus is right to give this argument short shrift. Mr Bush did more than any other American president—certainly more than the sainted Ronald Reagan—to give the various divisions of the conservative army what they wanted: tax cuts for the anti-government brigades; a ban on stem-cell research for the evangelicals; war with Iraq for the neoconservatives. The subsequent mess revealed the movement's internal incoherence and the difficulty of turning a protest movement into a governing coalition.

The author argues that the debacle has been a long time a-coming. Over the past 50 years or so American conservatives have transformed themselves into latter-day Jacobins—slogan-spouting ideologues who want to destroy government rather than reform it. They are so blinded by partisanship that they are incapable of seeing any vices in their own side or any virtues in their opponents, and so consumed by anger that they define themselves by what they want to destroy rather than to preserve. American conservatism is dying as a movement precisely because it has abandoned the principal insights of classical conservatism: for example, that government is a precondition for civilisation.

It is hard not to sympathise with Mr Tanenhaus's distaste for the likes of Bill O'Reilly, a commentator from the populist right. But his analysis is nevertheless unsatisfactory. Part of the problem lies in balance. Mr Tanenhaus has lots of fascinating things to say about the early contributors to the *National Review*, the magazine founded by Buckley. But he tells us little about the right's more recent reactions to big structural changes in American society, such as the browning of the population. His book is all preface and no body.

Then there is his otherworldliness. Mr Tanenhaus has no time for the shrillness of the political right. But what about the shrillness of the political left? He condemns the conservative movement for its anti-government fundamentalism. But doesn't somebody need to be pushing in the opposite direction from all those empire-builders in the bureaucracy? "The Death of Conservatism" is essentially an appeal for unilateral disarmament by the right masquerading as a fair-minded report on the state of the battle.

Brazilian literature

The slide towards insecthood

Aug 20th 2009
From The Economist print edition

Why This World: A Biography of Clarice Lispector. By Benjamin Moser. *Oxford University Press; 496 pages; $29.95. Haus; £20.* Buy from Amazon.com, Amazon.co.uk

"PREHUMAN divine life is a life of singeing nowness." Clarice Lispector, who wrote these words, was as enigmatic as they are. Benjamin Moser sets out to crack the enigma. One finishes his new biography largely persuaded by his solution while wishing that he had gone at the task a little less strenuously.

Haus Publishing

If only we could understand

Lispector, the "princess of the Portuguese language" and perhaps the first Latin American writer to be identified as a practitioner of magic realism, is one of the more obscure geniuses of modern letters. A Brazilian Jew, she fashioned strange, experimental novels and stories in elemental settings that seem only tangentially related either to Brazil or to Judaism. She proclaimed her Brazilianness more often and more forcefully than her Jewishness. But Mr Moser believes that her work is profoundly Jewish. He makes the case that her tragedies and philosophical concerns led her to create a body of work that belongs within the tradition of Jewish mysticism.

Lispector was born in Ukraine to a family still reeling from the pogroms and plagues that followed the first world war and the creation of the Soviet Union. Her feet never touched Ukrainian soil, she insisted—she was a year old when the family fled. Her intellectually ambitious father turned to peddling in Brazil's poor north-east. Her mother, a secret writer herself, died slowly from syphilis caught from rape in the old country.

Legendarily beautiful, Lispector embarked on a conventional life, marrying a diplomat and mothering two sons. She was not above purveying make-up tips through ladies' columns in newspapers. But the corseted, wandering life of a diplomat's wife did not suit her and one son was schizophrenic. She divorced and returned to Rio de Janeiro to live out her days. A fire caused by sleeping pills and cigarettes scarred her beauty.

For Mr Moser, Lispector's earliest traumas were the most important. Storytelling began as a way of willing her mother's recovery. The narrative compulsion was coupled to the unsettling intuition that humans have no secure place along the continuum of creation; they slide toward insecthood even as they grope for an absent God. Lispector has been compared to Jean-Paul Sartre, for her sense of life's senselessness, and to Franz Kafka. "The Passion According to G. H." (from which the quotation at the start of this review is taken) has the Kafkaish plot of an encounter between a woman and a cockroach.

Mr Moser emphasises Lispector's debt to Hermann Hesse's "Steppenwolf", who is part divine and part diabolical, and to Baruch Spinoza, who saw God as having an amoral, indifferent nature. Above all, he sees Lispector as a latter-day cabbalist for whom utterance itself is the act of creation: for her, God is among those thus created.

Lispector did not choose to say much about herself directly. Mr Moser's biography relies therefore on inference, context and interpretation. His primary sources for the writer's early life are an autobiographical novel and memoir by her sister, Elisa. The family lived through a tumultuous period of Brazil's history, during which Jews sometimes had reason to feel menaced by bigoted despots and fascist rabble. But in his eagerness to emphasise the anxiety that the Lispectors must have felt, Mr Moser underplays Brazil's tradition of racial and cultural mixing.

At times, Mr Moser's attempt to understand Lispector as a Jewish writer can feel like recruiting. Lispector was never obvious, as Mr Moser notes. This absorbing and perceptive biography of a fascinating writer sometimes is.

New film: “District 9”

Prawns and other illegal aliens

Aug 20th 2009 | LOS ANGELES
From The Economist print edition

Unlike recent sci-fi blockbusters, this is a clever film with a satirical edge

THIS science-fiction film from South Africa asks us to believe one impossible thing at the outset. In 1989 a giant flying saucer stalled in the sky over Johannesburg and has been hanging there ever since; its occupants, a motley herd of bandy-legged crustaceans, have been crammed into one of the townships once reserved for blacks. It is now 2010, and friction between the newcomers and the South Africans, who derisively refer to their unwanted guests as “prawns”, has grown to the point where the inhabitants of District 9 have to be resettled. If you can suspend belief on those points, and don’t flinch from the sight of blood and violence, you are ready to embark on a Swiftian rollercoaster with Neill Blomkamp, a South African-born director whose first film (playing now in America and due to open in Europe soon) looks set to catapult him into fame.

Mr Blomkamp’s protagonist is a fool named Wikus van der Merwe (Sharlto Copley), a senior employee of the multinational security company to whom supervision of District 9 has been outsourced. Blindly paternalistic in his dealings with his surly, distrustful charges, Wikus grins vapidly while his colleagues invade their homes and beat them if they resist. But after ingesting a mysterious fluid, he himself starts turning into a prawn and spends the rest of the film being pursued by his employers who want to experiment on him. The film’s outrageous deadpan humour recalls the early efforts of its producer, Peter Jackson. Clearly, the hobbits and wizards of “The Lord of the Rings” are not all that Mr Jackson has up his cinematic sleeve.

Paying tribute to the grungy, violent science fiction of the 1980s, like “Terminator” or “RoboCop”,“District 9” revives the tradition of satirical comment that once enlivened the genre before globe-straddling film-makers started producing over-advertised extravaganzas spawned by toys (Mr Blomkamp’s budget would barely pay the catering bill of one of the summer’s blockbusters). The aliens’ camp was built in an abandoned black township near Soweto, re-using the materials of huts that had been left standing. This further contributes to the lived-in look of everything in “District 9”, including that enigmatic hovering spaceship, which the prawns appear to have been using to hang out their washing.

But critics who have concluded that Mr Blomkamp’s satire is aimed at apartheid because his film is set in South Africa should brush up on the living conditions to which the world’s refugees, displaced people and other vulnerable groups are currently being subjected. The sight of soldiers roughing up and humiliating the alien prawns—who just want to be left alone to forage in the black-market for cat food, their favourite delicacy—may convey something sharp about the treatment of 42m uprooted terrestrials.

The Tiananmen uprising

Spied from the inside

Aug 20th 2009
From The Economist print edition

Tiananmen Moon: Inside the Chinese Student Uprising of 1989. By Philip Cunningham. *Rowman & Littlefield; 304 pages; $39.95 and £24.95.* Buy from Amazon.com, Amazon.co.uk

THE great virtue of Philip Cunningham's book about the Tiananmen uprising is that he took part in it. Most accounts of the Chinese student uprising, which started in April 1989 and ended seven weeks later in June with the killing of several hundred protesters and onlookers in Tiananmen Square, have been by outsiders, even if they were witnesses to the slaughter in the square. Moreover, since Beijing was so much the centre of the drama, there has been little informed writing about what was going on in hundreds of other Chinese cities, involving at least 1m demonstrators.

EPN

Soldiers v students

Mr Cunningham, an American who now teaches media studies in Japan, was a university student in Beijing after having studied Chinese politics at home. He saw the unfolding of the demonstrations on university campuses in Beijing, sometimes as a participant, sometimes just watching.

He describes the resolve of the students, cheered on by tens of thousands of ordinary Beijing residents, to revive the spirit of earlier urban uprisings demanding change. (Some people believed that China's leader, Deng Xiaoping, and his colleagues were paralysed by the students' actions. But the memoirs of Zhao Ziyang, who was deposed as party secretary because of his sympathies with the students, show that six weeks before the killing, Deng was determined that the demonstrators should be "smashed".)

As Mr Cunningham notes, the students adopted gestures, slogans and beliefs almost as if they were taking orders from outside. The regime pounced on this, declaring it to be proof that there was a "black hand" behind the scenes manipulating the demonstrators. Although he initially wondered about outside influence, Mr Cunningham rejects the charge, suggesting instead that centuries of Chinese manners and Communist indoctrination gave an autopilot quality to much of what the students believed and did. At the same time, he is very good at describing the rivalries of some of their leaders, their vanities and their imitation of the Communist Party itself in their secrecy and hierarchy.

There are several things wrong with the book. It lacks, for instance, a concise outline of how the movement began and how it turned rebellious. And there are pages of direct discourse which Mr Cunningham purports to recall verbatim. He became an interpreter for the BBC and derides the network's obsession with finding English-speakers and good pictures. But the broadcasts, produced by Mark Thompson, the BBC's current director-general, and which Mr Cunningham appears not to have seen, turned out to be excellent.

However much he took part, Mr Cunningham was always reminded that he was a *lao wai*, a foreigner. There would be somebody in the square who would keep shouting: "Watch the foreigner run, sit, eat." He was also a bit late in the day since the demonstrations had begun two weeks before he joined them. "Tiananmen Moon" has faults. But there is still much to be learnt from it: it is a worm's-eye view by a keen-eyed worm.

Les Paul

The man who changed rock music

Aug 20th 2009
From The Economist print edition

Les Paul, a pioneering rock musician and inventor, died on August 13th

Corbis

How high the moon

UNTIL about two months ago a short, slightly bent 93-year-old man would take to the stage every Monday in a New York nightclub. He would place a guitar bearing his name under a right arm permanently set at a right angle, touch the strings with the few working fingers of his arthritic hands and launch into some of the greatest guitar riffs of all time. Few musicians have careers lasting more than eight decades. Even fewer can boast two huge accomplishments. Les Paul, who died last week, invented both the electric guitar and multi-track recording, inventions that changed the sound and production of rock music.

Lester Polsfuss was born in a small town in Wisconsin in 1915. He taught himself the harmonica, banjo and guitar, sometimes building the instruments out of materials he found. He made his first open-bodied electric guitar by attaching a pickup from an old Victrola. Soon he changed his name to Les Paul and began playing in local hillbilly music bands.

Before long Mr Paul was performing with the most elegant bands on radio and in posh nightclubs. In the 1940s he played and recorded with all the big names of the era including Nat King Cole, Rudy Valée and Kate Smith. Dissatisfied with the sound of amplified guitars, he used a piece of railway sleeper to make a solid base for the strings and pickups, producing in this way a unique tone. The "log", as he called it, was the first solid-body electric guitar.

After the war he started experimenting with recording techniques, altering the pitch and resonance of notes. After some 500 tries, he produced a recording that combined two versions he had played of "Lover", a song that topped the charts in 1948. Shortly afterwards he was injured in a car crash and doctors could do nothing with his crushed right arm except lock it in one position. Without hesitation he told them to set it in a position to play the guitar.

A year earlier he had teamed up with Mary Ford, a country singer whom he later married. Sculpting her voice like clay, Mr Paul built layers of sound into one combination. Soon he was creating 24-track recordings, including such hits as "How High the Moon" and "The World is Waiting for the Sunrise".

Dark days followed. For a time there were no musical geniuses to put his inventions to their best use. Mr Paul and Ms Ford were trapped in a 1950s television show in which they had to appear in suits and pearls on the patio of a suburban ranch house breaking into song by the barbecue grill. By the mid-1960s, his marriage over, Mr Paul felt music had passed him by. He turned to refining his recording technology. Also, at the request of the Gibson guitar company, he produced his signature Les Paul model, still the Cadillac of guitars.

But then a new generation of musicians discovered him and his pioneering work for rock music.

Pilgrimages to honour the father of the electric guitar by stars such as Keith Richards, Eric Clapton and Paul McCartney made him famous again. He started playing in small clubs once more. A 2005 album, made with the help of admirers, including Sting, won two Grammies. Not at all a bad tribute for his 90th birthday.

Gayatri Devi

Aug 20th 2009
From The Economist print edition

Gayatri Devi, Maharani of Jaipur, died on July 29th, aged 90

Rex Features

THOUGH India has not been ruled by princes for many decades, it is not hard to find princesses about the place. Bollywood stars, for example, in sheaths, shades and bling, whose every move and change of wardrobe is recorded in flashy magazines; *fashionistas*, aping Kareena's T-shirt or Priyanka's bobbed hair, who spend their afternoons eating ice cream in Delhi's malls; and the VIPs, or VVIPs, who force their cars through the traffic with horns blaring, and who refuse the indignity of being searched at airports.

In contrast to these one may sometimes find, at high tea at the Delhi Polo Club or in the lounge of the Taj hotel, the genuine article. Gayatri Devi was among the most famous of these. Her beauty was astonishing, praised by Clark Gable, Cecil Beaton and *Vogue*, but liner or lipstick had nothing to do with it. She had a maharani's natural poise and restraint. From her grandmother, she had learned that emeralds looked better with pink saris rather than green. From her mother, she knew not to wear diamond-drop earrings at cocktail parties. A simple strand of pearls, a sari in pastel chiffon and dainty silk slippers were all that was required. The fact that she looked equally good in slacks, posing by one of the 27 tigers she personally eliminated, or perched, smoking, on an elephant, merely underlined the point. She was a princess, and a princess could make Jackie Kennedy appear almost a frump.

Money was never lacking in her life. As the daughter of Prince Narayan of Cooch Behar, in West Bengal, she grew up with dozens of staff and governesses recommended by Queen Mary. Thirty horses, six butlers and four lorryloads of luggage accompanied the family to their holiday cottage. "Broomstick", as the family called her—other members were "Bubbles" and "Diggers"—was polished up in Lausanne and Knightsbridge, where she rather redundantly took a secretarial course. Her future husband, the Maharajah of Jaipur ("Jai" to her) first appeared at Woodlands, the family home in Kolkata, resplendent in an open-top green Rolls Royce. When she married him in 1940 her presents included a Bentley, a hill-station house and a trousseau that was left for collection at the Ritz in Paris. Their life came to revolve round the polo seasons in which he starred: winter and spring in India, summer in Windsor or Surrey, the thundering chukkas interspersed with plentiful champagne.

Yet there was an oddity about Gayatri Devi. She was a tomboy who liked to keep company with the servants, worrying about their wages, and with the mahouts, learning their songs and stories of elephants. After meeting Jai at the age of 12 she began to wish she could be his groom, fortuitously

brushing his beautiful hand as she handed him his polo stick. Distinctions between *raja* and *praja*, prince and people, did not bother her, and she could be as cavalier about the yawning social divide between women and men. As Jai's third wife, she should have been in purdah in a "city" of 400 other lounging and sewing women, watching the world through filigree screens. Instead she kept him company in the palace, riding and big-game hunting, or flying to Delhi in her private plane to shop. And she set up a girls' school in Jaipur through which, she hoped, other daughters of the nobility might eventually learn to stick up for themselves.

The perfumed prison

Independence in 1947 brought a democratised India and the replacement of the 562 princely states with centralised, socialist government, but her attachment to "my people" did not change. Command, like style, came naturally to her. In both Cooch Behar and Jaipur, arriving becomingly wind-blown at the wheel of her Buick or her Ferrari, she would be greeted with flowers and incense and with deep prostrations in the dust. The villagers trusted her to help them, so she tried. That intimate understanding between ruler and ruled, she often said later, was sadly missing from modern India. It went with the crumbling of modern Jaipur which, under the maharajahs, had been a glorious desert city of wide avenues, palaces, peacocks and pink walls. She always saw it that way.

In 1960, having asked Jai's permission and summoned the party secretary to the palace, she joined the liberal Swatantra party to oppose Jawaharlal Nehru's left-wing Congress. She did not like socialism or five-year plans. A run for parliament two years later for the Rajasthan constituency gave her the world's largest landslide, 192,909 votes. But this was hardly surprising. The people were voting for "Ma", their princess, an exquisite figure in pearls and pale chiffon enthroned on a palanquin of carpets, who nevertheless called them her sisters and her brothers.

She continued to field their problems to the end of her life, though her political career as such did not long outlast a spell in Delhi's Tihar prison in 1975, under Indira Gandhi. The charge was currency offences, based on a few Swiss francs found in her bungalow among the jade, rose-quartz, Lalique and Rosenthal. The prime minister seemed mostly to object to her aristocracy. Gayatri Devi softened the blow by pouring French perfume into the open sewer in her cell. As it ran through the building, Asia's largest prison and one of its worst, other prisoners gathered to inhale the wafting vapours, the true scent of royalty.

Overview

Aug 20th 2009
From The Economist print edition

Japan's GDP grew by 0.9% in the three months to the end of June, an annualised rate of 3.7%. Stronger exports and a rise in consumer spending more than offset weakness in housing and business investment.

Industrial production in **America** rose by 0.5% in July compared with June, after a surge in the output of cars and car parts. The housing market was less buoyant. Private housing starts fell by 1% in July. The number of permits to build new homes fell by 1.8%.

Britain's inflation rate was steady at 1.8% in July. In much of the rest of the world **consumer prices** have fallen in the past year. America's were unchanged in July, leaving them 2.1% lower than in July 2008. In the euro area, consumer prices fell 0.7% in the year to July, revised from an initial estimate of a 0.6% decline. Canada's price index in July was 0.9% lower than a year earlier. And in Malaysia consumer prices fell by 2.4% in the year to July.

South Africa's GDP fell at an annualised rate of 3% in the three months to the end of June. That followed a 6.4% annualised decline in the first quarter.

Turkey's central bank reduced its benchmark interest rate by half a percentage point to 7.75% on August 18th. In a statement, the bank's seven-strong monetary-policy committee said recent indicators pointed to a "gradual and protracted" economic recovery. With inflation expected to stay low for a long period, the committee suggested that "further measured rate cuts" are likely.

Output, prices and jobs

Aug 20th 2009
From The Economist print edition

Output, prices and jobs

% change on year ago

	Gross domestic product				Industrial production	Consumer prices			Unemployment
	latest	qtr*	2009†	2010†	latest	latest	year ago	2009†	rate‡, %
United States	−3.9 Q2	−1.0	−2.6	+2.0	−13.1 Jul	−2.1 Jul	+5.6	−0.3	9.4 Jul
Japan	−6.4 Q2	+3.7	−6.4	+1.1	−23.5 Jun	−1.8 Jun	+2.0	−1.1	5.4 Jun
China	+7.9 Q2	na	+8.0	+8.0	+10.8 Jul	−1.8 Jul	+6.3	−0.6	9.0 2008
Britain	−5.6 Q2	−3.2	−4.2	+1.0	−11.0 Jun	+1.8 Jul§	+4.4	+1.8	7.8 May††
Canada	−2.1 Q1	−5.4	−2.2	+1.8	−11.8 May	−0.9 Jul	+3.4	+0.5	8.6 Jul
Euro area	−4.6 Q2	−0.4	−4.4	+0.6	−17.0 Jun	−0.7 Jul	+4.0	+0.5	9.4 Jun
Austria	−4.4 Q2	−1.7	−3.2	+0.2	−13.5 May	−0.2 Jul	+3.8	+0.5	4.4 Jun
Belgium	−3.8 Q2	+1.6	−3.5	+0.4	−17.3 May	−1.7 Jul	+5.9	+0.3	11.3 Jun‡‡
France	−2.6 Q2	+1.4	−2.8	+0.8	−12.8 Jun	−0.7 Jul	+3.6	+0.2	9.4 Jun
Germany	−5.9 Q2	+1.3	−5.9	+0.8	−18.0 Jun	−0.5 Jul	+3.3	+0.2	8.3 Jul
Greece	−0.2 Q2	+1.3	−3.1	−0.8	−11.4 Jun	+0.6 Jul	+4.9	+0.5	8.5 May
Italy	−6.0 Q2	−1.9	−5.1	+0.4	−21.9 Jun	nil Jul	+4.1	+0.8	7.3 Q1
Netherlands	−5.1 Q2	−3.4	−4.3	+0.7	−12.7 Jun	+0.2 Jul	+3.2	+1.3	4.8 Jul††
Spain	−4.1 Q2	−3.9	−3.9	−0.6	−14.5 Jun	−1.4 Jul	+5.3	−0.4	18.1 Jun
Czech Republic	−3.4 Q1	−12.9	−3.5	+1.2	−12.2 Jun	+0.3 Jul	+6.9	+1.5	8.4 Jul
Denmark	−4.1 Q1	−4.2	−3.9	+0.6	−18.6 Jun†††	+1.0 Jul	+4.0	+1.1	3.8 Jun
Hungary	−7.6 Q2	−8.1	−6.3	−1.0	−18.6 Jun	+5.1 Jul	+6.7	+4.3	9.6 Jun††
Norway	−4.8 Q2	−5.0	−2.0	+0.5	−6.3 Jun	+2.2 Jul	+4.3	+2.5	3.1 May***
Poland	+0.8 Q1	na	−0.8	+1.5	−4.6 Jul	+3.6 Jul	+4.8	+3.2	10.7 Jun‡‡
Russia	−10.9 Q2	na	−7.0	+2.5	−10.8 Jul	+12.0 Jul	+14.7	+12.2	8.3 Jun‡‡
Sweden	−6.2 Q2	−0.1	−4.9	+1.3	−20.8 Jun	−0.9 Jul	+4.1	−0.2	9.8 Jun‡‡
Switzerland	−2.4 Q1	−16.0	−2.3	+0.4	−9.4 Q1	−1.2 Jul	+3.1	−0.5	3.9 Jul
Turkey	−13.8 Q1	na	−5.6	+2.3	−9.7 Jun	+5.4 Jul	+12.1	+6.2	13.6 May‡‡
Australia	+0.4 Q1	+1.5	nil	+1.8	−3.6 Q1	+1.5 Q2	+4.5	+1.7	5.8 Jul
Hong Kong	−3.8 Q2	+13.9	−5.4	+2.6	−10.2 Q1	−0.9 Jun	+6.1	nil	5.4 Jul††
India	+5.8 Q1	na	+5.5	+6.3	+7.8 Jun	+9.3 Jun	+7.7	+6.0	6.8 2008
Indonesia	+4.0 Q2	na	+2.6	+3.4	+0.2 Jun	+2.7 Jul	+11.9	+4.3	8.1 Feb
Malaysia	−6.2 Q1	na	−5.0	+3.3	−9.6 Jun	−2.4 Jul	+8.5	−0.3	4.0 Q1
Pakistan	+2.0 2009**	na	+3.7	+2.8	−11.0 May	+11.2 Jul	+24.3	+12.0	5.2 2008
Singapore	−3.5 Q2	+20.7	−6.2	+3.2	−9.3 Jun	−0.5 Jun	+7.5	−0.2	3.3 Q2
South Korea	−2.5 Q2	+9.7	−1.8	+2.0	−1.2 Jun	+1.6 Jul	+5.9	+2.6	3.8 Jul
Taiwan	−10.2 Q1	na	−6.5	+0.6	−11.4 Jun	−2.3 Jul	+5.8	−1.3	5.9 Jun
Thailand	−7.1 Q1	−7.3	−4.5	+2.1	−7.8 Jun	−4.4 Jul	+9.2	−1.0	2.4 May
Argentina	+2.0 Q1	+0.2	−3.5	+0.5	−2.7 Jun	+5.5 Jul	+9.1	+6.2	8.4 Q1‡‡
Brazil	−1.8 Q1	−3.3	−1.0	+2.7	−10.9 Jun	+4.5 Jul	+6.4	+4.9	8.1 Jun‡‡
Chile	−4.5 Q2	−1.4	−1.2	+3.0	−8.3 Jun	+0.3 Jul	+9.5	+2.2	10.7 Jun††‡‡
Colombia	−0.6 Q1	+0.9	−1.0	+2.5	−6.5 May	+3.3 Jul	+7.5	+4.8	11.4 Jun‡‡
Mexico	−8.2 Q1	−21.5	−7.1	+2.8	−10.6 Jun	+5.4 Jul	+5.4	+5.5	5.2 Jun‡‡
Venezuela	+0.3 Q1	na	−4.2	−2.7	+11.4 Mar	+28.3 Jul	+33.7	+28.0	7.7 Q2‡‡
Egypt	+4.3 Q1	na	+4.4	+4.0	+5.8 Q1	+9.8 Jul	+22.2	+9.7	9.4 Q1‡‡
Israel	+0.1 Q2	+1.0	−1.3	+1.5	−8.6 Jun	+3.5 Jul	+4.8	+2.8	7.6 Q1
Saudi Arabia	+4.5 2008	na	−1.0	+3.3	na	+5.2 Jun	+10.6	+4.3	na
South Africa	−2.8 Q2	−3.0	−2.2	+3.1	−17.1 Jun	+6.9 Jun	+12.2	+7.1	23.6 Jun‡‡
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*									
Estonia	−16.6 Q2	na	−13.0	−3.0	−30.1 Jun	−0.7 Jul	+11.1	−0.8	17.0 Jun
Finland	−7.6 Q1	−10.3	−5.7	−0.1	−20.3 Jun	−0.6 Jul	+4.3	+0.1	8.8 Jun
Iceland	−3.9 Q1	−13.6	−6.5	+0.4	+10.1 2008	+11.3 Jul	+13.6	+12.5	8.1 Jun‡‡
Ireland	−8.5 Q1	−5.7	−7.7	−2.6	+2.6 Jun	−5.9 Jul	+4.4	−3.6	12.2 Jul
Latvia	−18.0 Q1	na	−17.0	−4.0	−18.5 Jun	+2.5 Jul	+16.6	+3.0	16.3 May
Lithuania	−22.4 Q2	−40.8	−15.0	−4.5	−16.3 Jun	+3.0 Jul	+12.2	+5.3	9.3 Jun‡‡
Luxembourg	−5.5 Q1	−5.9	−4.9	−0.8	−25.9 Apr	−0.3 Jun	+4.3	+0.5	5.4 Jun‡‡
New Zealand	−2.2 Q1	−2.7	−2.1	+0.7	−11.4 Q1	+1.9 Q2	+4.0	+1.8	6.0 Q2
Peru	−2.1 Jun	na	+1.3	+2.7	−8.6 May	+2.7 Jul	+5.8	+3.5	8.3 Jun‡‡
Philippines	+0.4 Q1	−8.9	−1.0	+3.7	−13.0 May	+0.2 Jul	+12.3	+2.9	7.5 Q2‡‡
Portugal	−3.7 Q2	+0.7	−4.1	−0.4	−9.5 Jun	−1.5 Jul	+3.1	−0.7	9.1 Q2‡‡
Slovakia	−5.3 Q2	na	−5.5	+0.7	−19.6 Jun	+2.5 Jul	+4.9	+1.8	12.1 Jul‡‡
Slovenia	−8.5 Q1	na	−6.0	nil	−22.3 Jun	−0.6 Jul	+6.9	+1.1	9.1 Jun‡‡
Ukraine	−20.3 Q1	na	−17.0	+1.0	−27.5 Jun	+15.5 Jul	+26.8	+16.0	2.4 Jun
Vietnam	+4.5 Q2	na	+4.2	+4.8	+7.6 Jul	+3.3 Jul	+27.0	+5.6	4.6 2007

*% change on previous quarter, annual rate. †*The Economist* poll or Economist Intelligence Unit estimate/forecast. ‡National definitions.- §RPI inflation rate -1.4 in July. **Year ending June. ††Latest three months. ‡‡Not seasonally adjusted. ***Centred 3-month average

Sources: National statistics offices and central banks; Thomson Reuters; Centre for Monitoring Indian Economy; OECD; ECB

The Economist commodity-price index

Aug 20th 2009
From The Economist print edition

The Economist commodity-price index
2000=100

	Aug 11th	Aug 18th*	% change on one month	% change on one year
Dollar index				
All items	198.6	189.8	+3.6	-20.3
Food	207.5	192.8	-2.0	-21.0
Industrials				
All	187.0	185.9	+12.4	-19.3
Nfa†	146.5	143.0	+4.6	-23.9
Metals	209.2	209.3	+15.6	-17.4
Sterling index				
All items	182.5	174.1	+3.2	-10.2
Euro index				
All items	129.9	124.4	+4.5	-16.9
Gold				
$ per oz	943.75	935.30	-1.4	+17.0
West Texas Intermediate				
$ per barrel	69.38	69.18	+6.8	-39.6

*Provisional †Non-food agriculturals.

The Economist commodity-price index

Aug 20th 2009
From The Economist print edition

Commodity prices have risen by almost 30% in dollar terms since the start of this year. Resurgent Chinese demand underpinned especially rapid rises for industrial commodities, the prices of which have increased by more than 55% since December. Copper and nickel prices have doubled to reach 11-month highs. Increases in food prices were attenuated by big harvests. Wheat and maize prices have fallen to eight-month lows. The United States Department of Agriculture estimates this year's soyabean and maize crops will be the largest and second- largest ever, respectively. But the price of sugar recently hit a 28-year high after poor rainfall in India and too much in Brazil spoiled their crops.

Trade, exchange rates, budget balances and interest rates

Aug 20th 2009
From The Economist print edition

Trade, exchange rates, budget balances and interest rates

	Trade balance* latest 12 months, $bn	Current-account balance latest 12 months, $bn	Current-account balance % of GDP 2009†	Currency units, per $ Aug 19th	Currency units, per $ year ago	Budget balance % of GDP 2009†	Interest rates, % 3-month latest	Interest rates, % 10-year gov't bonds, latest
United States	−639.5 Jun	−628.3 Q1	−3.0	–	–	−13.7	0.26	3.47
Japan	+9.0 Jun	+115.3 Jun	+2.5	93.7	110	−7.9	0.40	1.35
China	+269.4 Jul	+426.1 Q4	+6.5	6.83	6.85	−4.1	1.74	3.77
Britain	−139.8 Jun	−52.5 Q1	−1.7	0.61	0.54	−14.4	0.80	3.71
Canada	+15.5 Jun	−3.9 Q1	−2.3	1.10	1.06	−2.3	0.22	3.40
Euro area	−40.1 Jun	−158.1 May	−1.3	0.70	0.68	−6.4	0.85	3.29
Austria	−5.5 May	+10.7 Q1	+1.6	0.70	0.68	−5.2	0.86	3.68
Belgium	+6.3 May	−12.0 Mar	−2.4	0.70	0.68	−6.0	0.87	3.74
France	−71.1 Jun	−58.3 Jun	−2.1	0.70	0.68	−8.2	0.86	3.45
Germany	+182.0 Jun	+159.9 Jun	+3.7	0.70	0.68	−4.7	0.86	3.23
Greece	−50.6 Jun	−41.6 Jun	−9.0	0.70	0.68	−6.1	0.86	4.52
Italy	−11.9 May	−63.1 May	−2.8	0.70	0.68	−5.2	0.86	4.08
Netherlands	+43.5 Jun	+50.0 Q1	+6.1	0.70	0.68	−4.2	0.86	3.54
Spain	−101.4 May	−117.2 May	−7.1	0.70	0.68	−10.3	0.86	3.74
Czech Republic	+4.3 Jun	−4.7 Jun	−2.0	18.0	16.6	−4.8	1.89	5.14
Denmark	+6.2 Jun	+8.1 Jun	+1.5	5.23	5.06	−2.5	1.91	3.54
Hungary	+2.0 Jun	−11.3 Q1	−2.9	192	159	−3.9	8.40	8.80
Norway	+58.0 Jul	+79.6 Q1	+14.6	6.08	5.40	7.1	1.93	4.24
Poland	−13.5 Jun	−11.7 Jun	−3.3	2.93	2.25	−3.9	4.16	6.09
Russia	+122.2 Jun	+55.3 Q2	+1.9	31.9	24.4	−8.0	10.75	11.21
Sweden	+13.6 Jun	+31.4 Q1	+6.7	7.21	6.38	−4.7	0.10	3.39
Switzerland	+16.7 Jul	+56.6 Q1	+7.4	1.07	1.10	−3.1	0.34	2.00
Turkey	−47.4 Apr	−20.3 Jun	−0.4	1.50	1.19	−5.8	8.54	6.25‡
Australia	+5.7 Jun	−29.8 Q1	−4.0	1.21	1.15	−3.9	3.28	5.44
Hong Kong	−20.7 Jun	+29.6 Q1	+9.2	7.75	7.81	−3.9	0.22	2.30
India	−93.4 Jun	−29.8 Q1	−1.2	48.8	43.7	−7.8	3.35	7.60
Indonesia	+11.2 Jun	−0.8 Q1	+0.7	10,070	9,160	−3.0	7.06	6.85‡
Malaysia	+38.2 Jun	+40.5 Q1	+14.1	3.55	3.33	−8.0	2.14	2.14‡
Pakistan	−16.3 Jul	−12.2 Q1	−2.1	82.8	74.8	−4.3	12.30	12.22‡
Singapore	+18.4 Jul	+23.1 Q1	+14.4	1.45	1.41	−4.1	0.50	2.28
South Korea	+21.9 Jul	+20.7 Jun	+3.2	1,256	1,049	−5.0	2.48	5.37
Taiwan	+15.9 Jul	+31.9 Q2	+10.4	33.0	31.4	−5.2	0.85	1.34
Thailand	+11.3 Jul	+8.1 Jun	+5.2	34.1	34.1	−5.6	1.38	3.07
Argentina	+17.1 Jun	+6.8 Q1	+3.4	3.85	3.03	−0.9	14.25	na
Brazil	+27.1 Jul	−18.4 Jun	−1.3	1.85	1.62	−2.8	8.65	6.16‡
Chile	+4.5 Jul	−3.6 Q2	−0.5	553	519	−4.1	0.48	2.33‡
Colombia	−0.1 Jun	−6.5 Q1	−3.3	2,047	1,883	−3.0	5.13	5.68‡
Mexico	−16.0 Jun	−14.2 Q1	−2.7	12.9	10.1	−4.0	4.48	7.98
Venezuela	+32.5 Q1	+26.2 Q1	+1.4	6.58	0.00§	−7.6	14.51	6.55‡
Egypt	−26.1 Q1	−2.9 Q1	−1.8	5.56	5.36	−6.8	9.89	2.88‡
Israel	−8.7 Jul	+4.1 Q1	+2.2	3.82	3.57	−6.1	0.56	4.18
Saudi Arabia	+212.0 2008	+134.0 2008	+4.5	3.75	3.75	−0.5	0.64	na
South Africa	−5.4 Jun	−18.7 Q1	−5.3	8.05	7.76	−4.5	7.00	8.74
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*								
Estonia	−2.2 Jun	−0.5 Jun	+0.7	11.0	10.6	−3.5	5.83	na
Finland	+6.3 May	+3.1 Jun	+1.0	0.70	0.68	−2.6	0.84	3.55
Iceland	+0.7 Jul	−6.1 Q1	−5.9	128	82.8	−13.3	7.92	na
Ireland	+47.7 May	−11.3 Q1	−3.1	0.70	0.68	−12.9	0.86	4.68
Latvia	−3.8 Jun	−0.7 Jun	−2.0	0.49	0.48	−11.0	10.41	na
Lithuania	−3.9 Jun	−1.5 Jun	−0.3	2.43	2.34	−6.9	8.13	na
Luxembourg	−7.1 May	+2.2 Q1	na	0.70	0.68	−4.0	0.86	na
New Zealand	−2.3 Jun	−11.8 Q1	−7.1	1.49	1.41	−6.7	3.70	5.83
Peru	+2.3 Jun	−3.8 Q1	−2.3	2.96	2.91	−2.3	1.25	na
Philippines	−6.9 May	+5.1 Mar	+4.5	48.5	45.6	−3.1	4.19	na
Portugal	−28.2 Jun	−24.5 May	−8.8	0.70	0.68	−7.4	0.86	3.88
Slovakia	−0.3 Jun	−5.4 May	−7.0	21.2	20.6	−5.5	1.35	4.01
Slovenia	−2.9 Jun	−1.9 May	−1.6	0.70	0.68	−5.7	0.86	na
Ukraine	−13.4 Q1	−6.5 Q2	−0.5	8.35	4.61	−7.0	11.77	na
Vietnam	−5.4 Jul	−7.0 2007	−6.9	17,812	16,630	−9.0	8.20	6.30

*Merchandise trade only. †The Economist poll or Economist Intelligence Unit forecast. ‡Dollar-denominated bonds. §Unofficial exchange rate.

Markets

Aug 20th 2009
From The Economist print edition

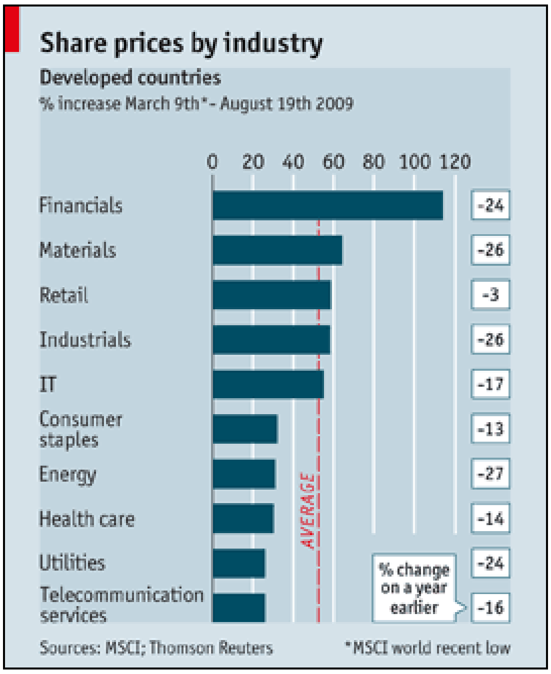
Markets

	Index Aug 19th	% change on one week	% change on Dec 31st 2008 in local currency	% change on Dec 31st 2008 in $ terms
United States (DJIA)	9,279.2	-0.9	+5.7	+5.7
United States (S&P 500)	996.5	-0.9	+10.3	+10.3
United States (NAScomp)	1,969.2	-1.5	+24.9	+24.9
Japan (Nikkei 225)	10,204.0	-2.2	+15.2	+11.4
Japan (Topix)	943.3	-1.7	+9.8	+6.2
China (SSEA)	2,923.6	-10.5	+52.9	+52.7
China (SSEB, $ terms)	187.4	-10.5	+69.2	+68.9
Britain (FTSE 100)	4,689.7	-0.6	+5.8	+21.4
Canada (S&P TSX)	10,686.8	+0.3	+18.9	+33.1
Euro area (FTSE Euro 100)	811.0	-1.9	+8.7	+11.1
Euro area (DJ STOXX 50)	2,622.9	-2.4	+7.2	+9.6
Austria (ATX)	2,346.5	+0.9	+34.0	+37.1
Belgium (Bel 20)	2,263.3	-0.4	+18.6	+21.3
France (CAC 40)	3,450.3	-1.6	+7.2	+9.7
Germany (DAX)*	5,232.0	-2.2	+8.8	+11.3
Greece (Athex Comp)	2,350.3	+2.4	+31.6	+34.6
Italy (S&P/MIB)	21,132.2	-1.9	+8.6	+11.1
Netherlands (AEX)	284.1	-1.7	+15.5	+18.1
Spain (Madrid SE)	1,116.9	-2.0	+14.4	+17.1
Czech Republic (PX)	1,123.6	+0.8	+30.9	+40.1
Denmark (OMXCB)	298.6	-1.4	+32.0	+35.0
Hungary (BUX)	18,213.6	+0.8	+48.8	+48.1
Norway (OSEAX)	345.4	-1.5	+27.8	+47.2
Poland (WIG)	35,599.9	+1.1	+30.7	+32.1
Russia (RTS, $ terms)	993.6	-3.1	+64.2	+57.2
Sweden (OMXS30)†	869.2	-0.9	+31.2	+43.9
Switzerland (SMI)	5,980.8	+0.3	+8.1	+7.9
Turkey (ISE)	45,645.0	+4.0	+69.9	+74.5
Australia (All Ord.)	4,387.5	+1.0	+19.9	+41.1
Hong Kong (Hang Seng)	19,954.2	-2.4	+38.7	+38.7
India (BSE)	14,809.6	-1.4	+53.5	+53.3
Indonesia (JSX)	2,277.8	-3.0	+68.0	+81.9
Malaysia (KLSE)	1,155.5	-2.1	+31.8	+28.6
Pakistan (KSE)	7,952.7	-1.3	+35.6	+29.6
Singapore (STI)	2,522.8	-1.9	+43.2	+42.4
South Korea (KOSPI)	1,546.0	-1.2	+37.5	+37.9
Taiwan (TWI)	6,788.6	-1.6	+47.9	+47.0
Thailand (SET)	631.3	-1.8	+40.3	+43.2
Argentina (MERV)	1,728.2	-2.5	+60.1	+43.7
Brazil (BVSP)	56,156.0	-0.8	+49.5	+88.4
Chile (IGPA)	15,440.0	-0.1	+36.3	+57.0
Colombia (IGBC)	10,474.1	+0.5	+38.5	+52.2
Mexico (IPC)	27,598.4	-1.8	+23.3	+32.3
Venezuela (IBC)	47,859.2	-0.9	+36.4	+46.8
Egypt (Case 30)	6,188.8	-1.5	+34.6	+33.6
Israel (TA-100)	870.7	-1.0	+54.4	+52.8
Saudi Arabia (Tadawul)	5,623.1	-3.8	+17.1	+17.2
South Africa (JSE AS)	24,259.5	-1.3	+12.8	+29.5
Europe (FTSEurofirst 300)	932.0	-1.1	+12.0	+14.6
World, dev'd (MSCI)	1,050.7	-0.7	+14.2	+14.2
Emerging markets (MSCI)	822.9	-2.1	+45.1	+45.1
World, all (MSCI)	266.6	-0.9	+17.1	+17.1
World bonds (Citigroup)	820.6	+1.6	+1.3	+1.3
EMBI+ (JPMorgan)	460.1	+0.6	+17.5	+17.5
Hedge funds (HFRX)§	1,103.3	+0.2	+8.1	+8.1
Volatility, US (VIX)	26.3	25.5	40.0	(levels)
CDSs, Eur (iTRAXX)‡	121.3	+9.9	-40.0	-38.6
CDSs, N Am (CDX)‡	177.7	+0.7	-23.9	-23.9
Carbon trading (EU ETS) €	14.9	+3.6	-7.8	-5.6

*Total return index. †New series. ‡Credit-default swap spreads, basis points.
Sources: National statistics offices, central banks and stock exchanges; Thomson Reuters; WM/Reuters; JPMorgan Chase; Bank Leumi le-Israel; CBOE; CMIE; Danske Bank; EEX; HKMA; Markit; Standard Bank Group; UBS; Westpac. §Aug 18th

Share prices by industry

Aug 20th 2009
From The Economist print edition



Anyone who had the confidence to buy shares in large international companies back in March, when markets had reached their lowest point to date in 2009, should be happy this week. The Morgan Stanley Capital International world index, which tracks the equity returns of the world’s 1,500 largest companies, has increased by more than 50% since March. Share prices of large financial firms have more than doubled. Longer-term investors who held their shares throughout the financial crisis, however, do not have as much to cheer about. Share prices in most industries are still around 20% lower than a year ago. Big retailers held up better than firms in any other sector. Their share prices fell by just 3%.